



Statement by

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Subcommittee on Government Management, Organization, and Procurement

Hearing on

The Federal Government's Consolidated Financial Statement

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Opening Statement

Thank you Chairman Towns, ranking member Bilbray, and members of the Committee for this opportunity to testify before you regarding the results of the Department of Homeland Security's (DHS) FY 2006 financial statement audit.

I also want to thank you for House Resolution 134. Your statement of support and recognition for the DHS workforce is greatly appreciated.

Regarding the audit, DHS received a disclaimer of opinion on its FY 2005 and FY 2006 financial statements. Secretary Chertoff and I are committed to correcting this and to achieving the intended outcome of the Department of Homeland Security Financial Accountability Act (DHS FAA), Public Law 108-330. To this end, the Department has put into action our plans to improve our financial management process and to address material weakness conditions such as those involving interagency and interdepartmental balances.

The task before us is not easy. But I am confident that working with the Congress, the Office of Management and Budget, and the Department's Inspector General, we will continue to make progress on our financial statement audit.

FY 2006 Financial Statement Audit Results

Substantial progress was achieved in our FY 2006 financial statement audit. Two components, U.S. Customs and Border Protection (CBP) and the Federal Law Enforcement Training Center (FLETC) received favorable audit outcomes. CBP obtained an unqualified opinion on all financial statements and FLETC achieved an unqualified opinion on its first ever balance sheet audit. Significant progress has also been achieved in reducing conditions that comprise the Department's material weakness structure. For example, most significantly the U.S. Immigration and Customs Enforcement (ICE) eliminated five of its seven component-level material weakness conditions. The Department is proud of these accomplishments and I am particularly grateful for the leadership of the Assistant Secretary for ICE, Julie Myers and the then ICE CFO Debra Bond. Their experience makes it clear that success comes from having strong

leadership support, and an effective corrective action plan. This year at the Department-wide level we have both.

Financial Management Improvement Initiatives

When I testified before this Committee, in September, I discussed with you the themes that I intended to build upon to achieve sustainable financial management improvement: People, Policy, Process, Systems and Assurance. I also outlined a series of initiatives I hoped to implement over the next year. I am pleased to report to you today that these efforts are well underway. For example:

- I talked about preparing the financial leaders of tomorrow and we are now concluding the first class of the CFO Mentorship program for mid-level managers. Over a four month period, these candidates have rotated through various components' CFO offices for breadth of experience and are undergoing an intensive leadership development course of study. We expect to begin a second class later this summer.
- I discussed ensuring a common set of skills and knowledge for all DHS financial management employees. Yesterday, was the first day of our New Hire training program for new financial management employees from throughout the Department. They will learn about the various parts of the Department; our core financial functions of budgeting and accounting; and the responsibilities of all financial management employees to support strong internal controls and to enforce compliance with fiscal law.
- Another initiative involved beginning the development of a financial management policy manual. This effort is well underway and we regularly conduct financial management policy workgroups with staff from across our components working together to develop Departmental level policy that will instill best practices and consistency in the execution of all DHS financial activity.
- Our plans for consolidating financial systems are moving forward. Rather than migrating all components to a new system, we are seeking to capitalize on existing compliant systems. This fall we migrated the

Domestic Nuclear Detection Agency onto the same system used by the Transportation Security Administration.

- We are currently interviewing for staff to create a management assurance team to ensure that the internal control improvements we put in place continue to work effectively and to identify and prevent waste, fraud, and abuse before it happens.

The Path Forward

I also discussed our intention of developing a corrective action plan to address the material weaknesses. That is also done. The Internal Controls Over Financial Reporting (ICOFR) Playbook outlines our strategy and process to resolve material weaknesses and build management assurances. Many of our material weaknesses were inherited and are longstanding challenges. These challenges will not be solved in a single step, but this ICOFR Playbook details the path forward through near and long-term fixes. The auditor's past reports highlight the challenges we face. They identified weaknesses that have occurred for a variety of reasons common to newly formed organizations, such as inconsistent processes, reliance on legacy policies, undeveloped internal controls, incomplete information, or systems that cannot properly process reliable data and information. Our Playbook has two tracks. The first track includes corrective actions for auditor identified weaknesses, such as Fund Balance with Treasury and Intragovernmental Balances. The playbook includes a second track where we examine and test the processes where no weakness was identified.

Our corrective action plans, thus address auditor-identified weaknesses. But, we are not stopping at simply fixing what the auditors find. One of the most important lessons learned from our initial years of implementing the DHS FAA involved shifting from just focusing on audit opinions or addressing auditor-identified issues to also building support for the Secretary's Assurance Statement by focusing on management-identified root causes and management-performed test work. Through our multi-year internal controls assessments, we are

documenting the design of our controls and we will then test their operating effectiveness.

I appreciate the support we have received from our Office of Inspector General as we developed and executed the Playbook. Through performance audits they have provided timely feedback on our corrective action plans and I look forward to their continued independent advice and essential cooperation.

Interagency and Interdepartmental Accounting

I appreciate the Subcommittee's attention to the challenge of interagency and interdepartmental Accounting, so let me spend some time on this particular challenge. DHS conducts business internally with DHS components and externally with other Federal agencies (i.e., trading partners) resulting in the reporting of interagency and interdepartmental receivables, payables, transfers, revenues and expenses. Federal accounting and reporting regulations require Federal agencies to routinely identify and reconcile these balances and transactions with trading partners to ensure balances properly eliminate in the government-wide and DHS consolidated financial statements.

The challenge is that the accountants normally do not have enough information about the transaction to quickly or easily determine which office in another government agency they need to go to, in order to reconcile or "eliminate" the transaction. It is referred to as elimination because when an agency reports an amount it is due, the respective paying agency must report the same amount owed to that agency. If the respective agency items match, the balances will eliminate or "net-out", when their respective financial statements are consolidated at a Departmental and then again at a Government-wide level. Given the thousands and thousands of transactions involved, numerous reporting methods, and the size of the agencies, reconciling interagency balances across the Federal government is a daunting and labor intensive task.

In FY 2005, our auditor identified a material weakness condition within interagency and interdepartmental accounting. The Department made progress on this front in FY 2006 by improving out-of-balance account conditions between

DHS components eliminating it as an auditor identified weakness, however much remains to be done to improve this internal effort. The challenge of reconciling transactions with other Departments is an even greater challenge.

This past summer we held a corrective action planning workshop to identify the root causes of interagency and interdepartmental accounting material weakness conditions. This included a lack of policies and procedures, an insufficient number of properly trained staff and systems that did not record transactions at the trading partner level. We have outlined the path forward in the ICOFR Playbook.

Interagency and interdepartmental accounting is an area we expect to substantially remediate in FY 2007. We have hired a subject matter expert on the issue from the Department of Treasury and we will actively participate in the Chief Financial Officers Council's Interagency Dispute Resolution Committee to resolve interagency transaction problems and we are grateful for the strong and continued leadership by OMB and the Department of Treasury.

Conclusion

DHS has made progress since our last hearing, and we are on track to make more progress this year as well. I appreciate the support we have received from our Office of the Inspector General. I also appreciate the support we have had from the Congress and this Committee. Thank you for your leadership and your continued support of the Department of Homeland Security.