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H.R. 2886, DEPARTMENT OF HOMELAND SECURITY FINANCIAL ACCOUNTABILITY ACT

HEARING

OF THE

SELECT COMMITTEE ON HOMELAND SECURITY
HOUSE OF REPRESENTATIVES

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H.R. 2886, DEPARTMENT OF HOMELAND SECURITY FINANCIAL ACCOUNTABILITY ACT

Wednesday, October 8, 2003

HOUSE OF REPRESENTATIVES,
SELECT COMMITTEE ON HOMELAND SECURITY,
Washington, DC.

The committee met, pursuant to call, at 1:05 p.m., in Room 2318, Rayburn House Office Building, Hon. Christopher Cox [chairman of the committee] presiding.

Present: Representatives Cox, Camp, Linder, Shadegg, Gibbons, Sweeney, Turner, Norton, McCarthy, Jackson-Lee, Pascrell, Christensen, Etheridge, Lucas, Langevin, and Meek.

Chairman COX. Good afternoon. A quorum being present, the committee will come to order. The committee is meeting today to consider the management and financial accounting controls at the Department of Homeland Security and legislation to bring the Department within the coverage of the CFO Act.

It was only 5 months ago this year that the Department opened its doors. The establishment of the Department of Homeland Security marks the largest reorganization of the Federal Government in history. It is a merger of 22 separate Federal agencies with more than $50 billion in assets, $36 billion in liabilities—although the accounting certitude of that figure is questionable—and roughly 180,000 employees.

The President created the new department not to achieve a new M&A standard, but rather to enhance our capabilities to prevent terrorism. It is this core mission to make our country safer that requires us to examine how the financial systems of 22 separate agencies will be consolidated in order to achieve our objective.

In conducting oversight of DHS, this committee must make financial accountability a top priority. This is necessary not only to ensure that taxpayer dollars are fully and accurately accounted for and spent prudently to achieve well defined and measurable objectives, and to prevent waste, fraud and abuse, but even more importantly, it is necessary so that the Department succeeds in its overall mission. That mission is of course protecting Americans.

Today, in keeping with other oversight mandates, we will examine the financial policies, processes and systems being utilized and being proposed for use at the Department. Our analysis is being conducted within the context of legislation now pending before this committee, H.R. 2886, the Homeland Security Financial Accountability Act.

In addition, we will explore the Department's steps towards a framework for strategic planning and program evaluation. Questions that we are interested in addressing today include how DHS will ensure that the appropriate amount of funds are requested for specific programs and how those programs will be held to performance standards.

H.R. 2886, the Department of Homeland Security Financial Accountability Act, contains a number of financial management provisions. It includes measures subjecting the Department to the statutory framework and reporting mandates of the CFO Act. It imposes additional financial audit opinion requirements.

I am interested to hear the views of our witnesses today—we have an outstanding panel—about the impact of the various provisions of the bill. It is my estimation that the Department is making solid progress in financial management.

Consolidating 22 separate agencies is no mean feat. But there is a broad plan to streamline and integrate financial systems and promote interoperability across the Department. I look forward to hearing your views on the panel about the progress of those initiatives today.

It is imperative, I believe, that the objectives of individual programs be firmly linked with the strategic plans of the Department. Budgetary requests must reflect the priorities of these strategic plans so that money is spent appropriately and with minimal, if any, redundancy. And, finally, the performance of department programs must be examined regularly by this committee to assist in implementation, to assess progress, and to best allocate future resources.

We already have laws in effect to promote the responsible use of scarce resources in the Federal Government. I think we need to use these laws to much greater effect. In 1993, Congress enacted the Government Performance and Results Act, which requires that every major Federal agency report their plans for future years and give an assessment of performance for previous years.

These reports provide the basis for Congress to assess how each agency is performing. Ensuring that these statutory requirements are fulfilled in the Department of Homeland Security is critical to allowing this committee to provide effective oversight in partnership with the Department. I am pleased the Department has established the Office of Program Analysis and Evaluation, under the CFO, Dr. Carnes, with the responsibility for integrating strategy, performance, management and budget for the entire Department.

The Department will need to rely on the best practices of established departments within the Federal Government as well as in the private sector while adapting these policies to meet the unique domestic security mission of the Department of Homeland Security. I dare say that back when we first wrote the CFO Act, and I was one of the original authors of the CFO Act, and I am a strong proponent of it, calling a hearing on the topic of financial accounting controls would likely not attract a good deal of attention.

I think in the post-Enron world that is not so. I think non-accountants now understand the importance of management control, or the purposes of achieving the objectives of an organization,

and also recognize the down side of not having a good system of financial controls in place in a large organization.

We want to make sure that we take every opportunity to improve the work of the Department of Homeland Security, to perfect it in its achievement of its mission, and we want to use financial controls to that end.

I thank the witnesses with us here today for providing us with your testimony in advance. I look forward to hearing the summary of your testimony in a moment and engaging in a colloquy with you. I now recognize the ranking member, Mr. Turner, for any opening statements that he may have.

PREPARED STATEMENT OF THE HONORABLE CHRISTOPHER COX, CHAIRMAN, SELECT COMMITTEE ON HOMELAND SECURITY

On March 1 of this year, we witnessed the standing up of the Department of Homeland Security, the largest reorganization of the federal government in history. The restructuring brought under one roof 22 separate federal agencies, more than $50 billion in assets, $36 billion in liabilities and roughly 180,000 employees. The President created the new Department, to enhance our capabilities to prevent terrorism, to protect our infrastructure against it, and to respond to any attack that might occur.

In conducting oversight of the Department of Homeland Security, this Committee must make financial accountability a top priority. We must insist that taxpayer dollars are fully and accurately accounted for. And we must ensure that every precaution is taken to prevent fraud, waste, and abuse.

It is imperative that the objectives of individual programs be firmly linked with the strategic plans of the Department. Budgetary requests must reflect the priorities of these strategic plans, so that money is spent appropriately and with minimal redundancy.

At one time these issues may have been considered dry, but in our post Enron debacle environment no one can discount their importance. Both the Executive branch and the Legislative branch of the federal government must fulfill our obligation to protect the taxpayer's bottom line.

Mr. TURNER. Thank you, Mr. Chairman. I appreciate you calling this hearing for the purpose of examining the financial planning and management practices of the Department of Homeland Security, and, specifically, to have a hearing on H.R. 2886, the Department of Homeland Security Financial Accountability Act.

Over the course of this fiscal year, the Department will spend around $30 billion on a wide range of programs and activities designed to keep this country safe from terrorism. It is important, I think, that the Department have all of the tools and the practices necessary to ensure that taxpayer dollars are spent efficiently and effectively. Also, I think it is important that these tools allow the Department to provide the Congress with all of the information that we need to carry out our responsibilities.

I am encouraged by several steps that I have seen the Department take recently in laying the groundwork for sound fiscal management. Among these are the establishing of a planning and programming and budgeting system similar to what has existed within the Department of Defense for many years to help in developing its 5-year budget plan, the creation of a Program Analysis and Evaluation Office to review program and budget requirements and analyze them in the context of an assessment of key threats and vulnerabilities; also, setting up an investment review board and a joint requirements review process to monitor the Department's progress in developing major programs and making related acquisition decisions. Each of these are good first steps.

Mr. Chairman, I think we all agree, however, that there is much more that must be done to be sure that we make the right choices regarding the security of our nation. The most important task I think that the Department has yet to accomplish is the development of a comprehensive threat and vulnerability assessment.

It seems that from testimony that we have had from Assistant Secretary Liscouski that such an assessment is some years away. I believe he estimated perhaps 5 years away. This, in my judgment, is unacceptable. Without a threat and vulnerability assessment, we cannot possibly decide how to allocate valuable funding between a variety of options such as cargo screening, improving the electrical grid, increasing bioterrorism protection, or tending to some other vulnerability.

At the Department of Defense, each installation assesses its vulnerabilities every year so security changes can be based on a current assessment of risk. But with the Homeland Security Department right now, we are in essence driving down the road without a road map to tell us where to go. Indeed, without a true threat and vulnerability assessment, we run the risk of trying to protect everything equally, which means we protect nothing effectively, or, worse yet, we end up funding programs based on current events or media attention rather than on rational evaluation of risk.

A threat and vulnerability assessment should be part of an updated annual Homeland Security strategy. An updated strategy could serve, in turn, to articulate the administration's goals across the government, better define our capabilities and needs and provide clear guidance to the budget planning process.

We all know that the threats we face are real, and the decisions we make today will decide our security tomorrow. Right now we are making our decisions without a good road map.

Mr. Chairman, I think we also need to ensure that the Department has a robust financial management system in place as provided for, in part, by the legislation that we are looking at today.

Such financial systems can also assist the Department in developing specific performance goals and benchmarks that can be used to evaluate whether it is in fact achieving the high goals that we have set for it.

And finally, Mr. Chairman, we must insist in the coming years that the Congress be provided with accurate, detailed budget information that it needs to carry out its oversight work. The Department's fiscal year 2005 request, which will arrive on our door step only about 4 months from now, must be sufficiently comprehensive to allow us to fully understand the required costs of homeland security. Such materials were not provided with last year's request.

If we believe that information is lacking, we should ask the hard questions and take the necessary steps to ensure that we have what we need.

Finally, Mr. Chairman, while great progress I think is being made, we know the task ahead will be difficult and much work remains to be done.

I appreciate each of the witnesses who are with us today. I appreciate your commitment to the security of our country, and I thank you for being with us today.

Thank you, Mr. Chairman.

Chairman COX. Mr. Gibbons, do you wish to be recognized for an opening statement?

Mr. GIBBONS. Mr. Chairman, in view of the importance of our witnesses' testimony today and the significance of which this committee views its interest in this subject, I am going to waive my opportunity to make an opening remark. I will submit them for the record at a later date. I want to thank you for your leadership on this issue and look forward to the testimony of the witnesses.

Thank you.

Chairman COX. Does any member on the minority side wish to be recognized for purpose of an opening statement?

Mr. ETHRIDGE. Mr. Chairman, I will submit mine for the record and waive.

Chairman COX. Thank you. If not, we can jump right into the testimony of our witnesses. I will recognize you in turn. We will begin with Dr. Bruce M. Carnes, the Chief Financial Officer for the Department of Homeland Security. As we mentioned, we have your written submission, and you are free to summarize your testimony as you see fit.

STATEMENT OF DR. BRUCE CARNES, CHIEF FINANCIAL OFFICER, DEPARTMENT OF HOMELAND SECURITY

Mr. CARNES. Thank you, Mr. Chairman. I will summarize my statement. Mr. Chairman, Mr. Turner, members of the select committee, I am delighted to be here to discuss our progress and the challenges in building financial management business and program evaluation processes at DHS.

As the CFO at the Department of Homeland Security, I am committed to building financial policies, processes and systems that are a model for the Federal Government. Much has already been done in the few months that we have been in existence to bring the financial policies, processes and systems of 22 disparate organizations into one department.

In March, we successfully transferred more than $50 billion in assets, $36 billion in liabilities and 180,000 employees to the Department. Within a few weeks we created the financial structures and support systems necessary to support these transfers. We have also launched a consolidated bankcard program that will reduce the number of programs within the Department from 27 to 3, created an investment review board to evaluate acquisitions above $5 million.

We are requiring certified project managers. We have development a joint requirements council. We have created an investment review board. We have initiated a 5-year budget and planning program; established a budget process modeled after DOD's POM process, program objectives memorandum process; launched a consolidated business and financial management systems program; and created a program analysis and evaluation organization.

We are developing a future years homeland security program and a strategic plan. All of these activities have been accomplished by a handful of outstanding and dedicated staff that I am very fortunate to be in charge of, and my task is to get out of their way and let them do their jobs. They are doing them spectacularly.

When we stood up, we inherited 22 disparate financial processes. We have consolidated them to nine, primarily by terminating memos of understanding with legacy agencies and shifting the workload to in-house financial support units. We are studying ways to streamline the financial processes used by DHS, with a goal of enhancing efficiency, reducing costs, and improving the quality of financial data.

We have 83 financial management systems, few of which are integrated. Some are outdated, lack functionality and are expensive to operate and maintain. To tackle this problem, we have launched an aggressive problem to transform DHS's business and financial management policies, processes and systems.

As part of this, we will develop and implement a departmental business and financial enterprise solution that results in a single suite of financial management systems for the Department. The objective of this program is to provide the business equivalent of a global positioning system for our operators and to provide CFO compliance and information for the Congress, the Treasury, and OMB and auditors.

We are launching a comprehensive review of the finance and accounting operations of all DHS components. This will include an assessment of performance standards, business processes, workload requirements, systems capabilities, staffing requirements and productivity levels. It will provide recommendations for establishing department-wide performance standards, improved business processes, possible consolidations of operations and systems improvements. Action plans will be developed to implement those recommendations.

Another challenge we face is preparing consolidated financial statements within the time frame established by OMB. This is a formidable challenge, but early on we decided that we needed to move aggressively to comply. We have submitted our interim statements to OMB on time, and we expect to have our fiscal year 2003 statements completed ahead of schedule.

Part of the challenge that we face in preparing our statements is mitigating the impact of 18 inherited material weaknesses that were identified in audits of the agencies that became the Department of Homeland Security. I have directed the Department's components to establish corrective action plans for each of these material weaknesses. We have established a system to monitor the implementation of those action plans. And these components report to me on a quarterly basis on their progress against them.

In addition, I am creating a unit within my organization to conduct internal audits, some of which will be focused on any material weakness that is not being corrected on schedule.

A word, if my might, about H.R. 2886. As the CFO of DHS, I applaud the spirit with which H.R. 2886 was introduced. I agree that increased accountability is important and necessary, as demonstrated by the continuing rash of corporate accounting scandals. But I want to assure the committee that as the Department's CFO, I have the same duties and responsibilities as CFOs in other agencies, and I am held accountable for ensuring the Department's financial integrity in the same manner.

The proposed legislation will not change the way I perform my job, nor will it give me any authority that I do not already have. Similarly the legislation will not change the requirements that the Department must comply with in accounting for its finances.

Section 3 of the bill requires that the Department submit a performance and accountability report that incorporates a program performance report. We will include program performance information in our fiscal year 2003 performance and accountability report. But that section also requires that the Department's report include an audit opinion of our internal controls, beginning in fiscal year 2005.

The bill mandates that the CFO Council and the President's Council on Integrity and Efficiency jointly conduct a study. An audit of internal controls could be costly and possibly redundant. The Department believes that the proposed study is necessary and that any decision to require DHS to audit its system of internal controls should await the outcome of that study.

One of the principal things I did when I went to DHS was to create a PA&E organization. I spent a number of years in DOD. And when I went from DOD to Energy, I created such an organization. I have created one at DHS.

We can get into its functions if you would like later on in the hearing, but it is one of the organizations within my shop of which I am most proud, and which is most essential to the development of our strategic plan and our future years homeland security program.

Thank you, Mr. Chairman. I will be happy to take your questions.

[The statement of Mr. Carnes follows:]

PREPARED STATEMENT OF BRUCE M. CARNES, CHIEF FINANCIAL OFFICER, DEPARTMENT OF HOMELAND SECURITY

Mr. Chairman, members of the Select Committee, I am pleased to be here to discuss our progress and challenges in building financial management, business and program evaluation processes at the Department of Homeland Security.

DHS Financial Management and Program Evaluation Accomplishments and Goals

The Department of Homeland Security was created to protect the American people by preventing terrorist attacks, reducing our vulnerability to attack, and minimizing the loss of life and speeding recovery should one occur. At the same time, the Administration saw the creation of the Department as an opportunity to build a model for management excellence by efficiently and effectively managing resources to deliver measurable results.

As the Chief Financial Officer at the Department of Homeland Security, I am committed to fulfilling this vision by building financial policies, process and systems that are a model for the Federal government. Just as we have consolidated border and transportation security functions, merged response activities, integrated terrorist threat intelligence, and coordinated homeland security research and development efforts, I believe we must with equal vigor transform our business practices and systems.

Since the Department was established, much has already been done to bring the financial policies, processes, and systems of 22 disparate organizations into one Department. In March 2003, we successfully transferred more than $50 billion in assets, $36 billion in liabilities, and more than 180,000 employees to the Department. Within a few weeks, we created the financial structures and support systems necessary to support these transfers. This was accomplished with only handful of staff—a remarkable achievement of which we are proud.

We have also launched a consolidated bankcard program that will reduce the number of programs within the Department from 27 to three, created an investment review board to evaluate acquisitions above $5 million, initiated a five-year budget and planning program, established a budget process modeled after the Department

of Defense's Program Objectives Memorandum process, launched a consolidated business and financial management systems program, and created a Program Analysis and Evaluation organization charged with leading the Department's program evaluation effort and ensuring compliance with performance and accountability requirements.

Our success in these areas has laid a solid foundation for our efforts to become a model of excellence in Federal financial management; however, much remains to be done. As we move forward, using the President's Management Agenda as our guide, we seek to:

- increase efficiency and effectiveness by producing financial data that is timely, reliable, and useful to decision makers;
- strengthen accountability by ensuring that internal controls are in place across the Department and appropriate oversight reviews are conducted;
- significantly reduce costs by consolidating functions, systems, and processes and by instituting best business practices; and .
- achieve results through the use of rigorous planning, measurement and evaluation processes.

These goals are ambitious and we face significant challenges in achieving them.

DHS Financial Management Challenges and Solutions

Consolidating the Department's 22 Financial Processes. Currently, the Department has 22 disparate financial processes. Several of these were established through memorandums of understanding with the Department's legacy agencies. Using these processes helped ensure sufficient financial support services were available when the Department was first established. However, they are labor-intensive and cumbersome to manage. Beginning October 1, 2003, we consolidated the number of processes from 22 to 10—primarily by terminating the memorandums of understanding with legacy agencies and by shifting the workload to in-house financial support service units.

This is only a good start. In FY 2004, we will consider options to further streamline the financial processes used by the Department with the goal of enhancing efficiency, reducing costs, and improving the quality of financial data.

Multiple and Redundant Financial Systems. The Department has 83 financial management systems, few of which are integrated. Some are outdated, lack functionality, and are expensive to operate and maintain. To tackle this problem, we have launched an aggressive program to transform the Department's business and financial management policies, processes, and systems.

As part of this initiative, we will develop and implement a departmental business and financial enterprise solution that results in a single suite of financial management systems for the Department. The objective of the program is to provide the business equivalent of a Global Position System that will:

- Provide decision-makers with the business information (e.g., budget, accounting, personnel, procurement, travel) they need in near real-time;
- Improve data quality and timeliness;
- Provide required information to our stakeholders, including the Office of Management and Budget, the Congress, the General Accounting Office, our Inspector General, and the public; and
- Help the Department obtain a clean opinion on our financial statements.

This program will have a major impact on the way the Department manages its business and financial operations and will result in the Department's becoming more efficient and effective by eliminating redundant systems and consolidating functions. Developing and implementing the envisioned suite of systems will require a substantial up-front investment; however, once implemented, we anticipate that this program will produce significant cost savings.

Lack of Standard Business Practices. Just as the Department has multiple financial systems and processes, we have multiple business practices for managing our financial operations. While some diversity is desirable to ensure that innovation thrives and best practices emerge, some standardization is also necessary.

Thus, we are launching a comprehensive review of the finance and accounting operations of all Department of Homeland Security components. The review will include an assessment of performance standards, business processes, workload requirements, systems capabilities, staffing requirements, and productivity levels. The review will also provide recommendations for establishing department-wide performance standards, improved business process, possible consolidations, and systems improvements. Action plans will be developed to implement recommendations. We anticipate that the Department will begin to realize cost savings from implementing the recommendations as early as FY 2005.

Challenges Relating to Coordination and Communication. In any organization as large as the Department of Homeland Security, communication and coordination can be a challenge. To tackle this problem, early in my tenure I established a departmental Chief Financial Officer's Council, which I chair, and whose members include the budget and finance directors from the Department's components. The Council has been instrumental in sharing information and priorities and for discussing the problems confronting the components.

While the Council has been effective in providing direction to the budget and finance officers, the fact remains that they are part of a different command structure. While this has not been detrimental to accomplishing the initiatives that we have pursued thus far, as we begin to make the sweeping changes needed to become a model for financial management excellence, working within the current structure could become a greater challenge.

Preparing Consolidated Financial Statements. Another challenge we face is preparing consolidated financial statements within the timeframe established by the Office of Management and Budget. Although this is a formidable challenge, we decided early on that the Department needed to move aggressively to meet the requirements of OMB Bulletin-01–09, as amended, which requires agencies to prepare financial statements. We have submitted our interim statements to OMB on time and expect to meet OMB's due date for the final audited statement.

Part of the challenge that we face in preparing our statements is mitigating the impact of 18 inherited material weaknesses that were identified in prior-year audits at the Department's legacy agencies. To tackle this problem, I directed the Department's components to establish corrective action plans for each material weakness. I also established a system to monitor implementation in which the components report to me on a quarterly basis on their progress in correcting their material weaknesses. In addition, I am creating a unit within my organization to conduct internal audits, some of which will be focused on any material weaknesses that are not being corrected on schedule. Through these processes, I believe that we will make significant progress in reducing the number of material weaknesses and ultimately eliminate them.

H.R. 2886 "Department of Homeland Security Financial Accountability Act"

As the CFO of the Department of Homeland Security, I applaud the spirit with which H.R. 2886, "Department of Homeland Security Financial Accountability Act", was introduced. I agree with the bill's sponsor, Congressman Platts, that increased accountability is important and necessary as demonstrated by the continuing rash of corporate accounting scandals.

While I agree with the overarching goal that H.R. 2886 seeks to accomplish, I believe that legislation may not be necessary. Section 2 of the bill proposes to subject the Department to the same financial management and accountability requirements as all other cabinet-level departments. It also proposes to change the status of the Chief Financial Officer from a presidential appointee reporting to an under secretary to a presidential appointee subject to Senate confirmation reporting to the Secretary.

As the Department's CFO, I have the same duties and responsibilities as CFOs in other agencies and am held accountable for ensuring the Department's financial integrity in the same manner. The proposed legislation will not change the way I perform my job nor will it give me any authority that I do not already have. Similarly, the legislation will not change the requirements the Department must comply with in accounting for its finances. The Department complies with the provisions of the Chief Financial Officers Act of 1990 and will continue to do so.

Section 3 of the bill requires that the Department submit a performance and accountability report that incorporates a program performance report. The Department will include program performance information in its FY 2003 performance and accountability report.

Also included in Section 3 is a provision that would require that the Department's performance and accountability report to include an audit opinion of the Department's internal controls over its financial reporting beginning in FY 2005. In addition, the bill mandates that the Chief Financial Officers Council and President's Council on Integrity and Efficiency jointly conduct a study of the potential costs and benefits of requiring agencies to obtain audit opinions of their internal controls over their financial reporting.

An audit of internal controls would be costly and very possibly redundant. The Department believes that the proposed study is necessary and that any decision to require the Department to audit its system of internal controls should await the results of the study.

Again, I support the intent of the proposed legislation. Should H.R. 2886 ultimately be enacted, the Department would look forward to working closely with the Congress on this important Issue.

Program Analysis and Evaluation

One of the first actions I took as the Department's Chief Financial Officer was to establish a Program Analysis and Evaluation (PA&E) Office and to recruit a highly experienced director to the lead organization. PA&E's primary responsibilities include:

- designing and managing the Department's Planning, Programming and Budgeting System;
- managing the development of the Future Years Homeland Security Program;
- coordinating the development of the Department's strategic plan;
- ensuring the Department meets performance-based budgeting requirements;
- managing the Department's Investment Review Process; and
- preparing the Department's Annual Performance Plan and the program and performance section of the annual Performance and Accountability Report.

The Department has made significant progress in each of these areas. We expect to issue a directive on the Department's new Planning, Programming and Budgeting System (PPBS) within the next month. The PPBS is being modeled after the Department of Defense's system and will include as an integral component guidance for establishing goals and performance measures which reflect program missions and assess desired outcomes. The PPBS will be the basis for developing the Department's first Future Years Homeland Security Program, which will be submitted to Congress in accordance with the provisions of the Homeland Security Act. We have made substantial progress on the Department's first strategic plan and expect to transmit a draft to Congress for review in early November. In the area of investment review, since May 2003, our Investment Review Board has evaluated approximately ten percent of the Department's major acquisitions (over $50 million) and will increase its efforts over the coming months. Under the leadership of the Deputy Secretary, the Department launched a comprehensive effort to develop measures of effectiveness to help assess performance and make more informed resource allocation and budget decisions. Finally, we are on track to issue on time the Department's first Annual Performance Plan, which will include rigorous performance measures for each of the Department's organizational elements. We will also publish the Department's first Performance and Accountability Report in January 2004.

We believe that through these initiatives we are taking the steps necessary to help improve performance, increase accountability and achieve the Department's mission.

Closing

In closing, I want to assure this committee that the Department of Homeland Security is advancing as rapidly yet judiciously toward our goal of becoming a model for management excellence. In the coming months, we will move aggressively to implement the plans that I have described for consolidation, streamlining, and increasing accountability. We will also announce further plans to help us reach these goals.

We look forward to working with the Congress as we progress with our plans and will seek your continued support as we move forward.

Chairman COX. Thank you. Our next witness is J. Richard Berman, Assistant Inspector General for Audits at the Department of Homeland Security.

STATEMENT OF J. RICHARD BERMAN, ASSISTANT INSPECTOR GENERAL FOR AUDITS, DEPARTMENT OF HOMELAND SECURITY

Mr. BERMAN. Chairman Cox, Ranking Member Turner, and members of the committee. Thank you for the opportunity to be here today to discuss financial management and program evaluation at the Department of Homeland Security and H.R. 2886.

On March 1, 2003, DHS was created by consolidating 22 domestic agencies to better protect the Nation against threats to the homeland. Each of the component agencies brought to DHS its distinct business processes as well as financial weaknesses. This presents DHS with significant challenges in integrating financial oper-

ations, creating a common infrastructure and developing goals, objectives and meaningful performance measures to guide and track progress.

Measures of effectiveness are critical to the process of evaluating the degree of success of department programs and operations, and making more informed resource allocation and budget decisions.

OIG will use the Department's goals and performance measures, as well as the President's management agenda in shaping its own work plans and priorities and will verify and validate program performance data as part of its audits and inspections.

In the area of financial systems and reporting, DHS must integrate and establish effective controls over the financial systems and operations of the incoming components, including correcting the weaknesses that it has inherited.

While some components, such as INS, have received unqualified audit opinions on their financial statements, they expended significant human resources and costs to prepare financial statements because of their inadequate financial systems and weaknesses in control.

DHS inherited a total of 18 material weaknesses identified in prior year financial statement audits at the legacy agencies, and we will be assessing these material weaknesses as part of our 2003 financial statement audit.

Information systems are another key area that DHS must address in order to establish sound financial management and business processes. This is an area in which opportunities abound to achieve greater economy and efficiency.

To meet these challenges DHS will need to build a unified financial management structure capable of supporting both efficient financial statement preparation and reliable, timely financial information for managing DHS's current operations, including information to support performance-based budgeting.

Grants and contracts management are also major areas of concern. DHS awards over $7 billion annually in grants under its emergency preparedness and disaster assistance grant programs, which were absorbed primarily from FEMA and the Department of Justice.

Previous FEMA and Justice OIG reports identified significant shortcomings in the preaward process, cash management, monitoring and grant closeout processes in the emergency preparedness programs.

Further, these programs have redundant or similar features, such as emergency planning, training, and equipment purchases and upgrades for State and local emergency personnel, and meaningful performance measures are desperately needed in these areas.

Additionally, FEMA's OIG found that FEMA had ineffective performance and financial oversight over disaster assistance grants. This, in turn, enabled grant recipients and subgrantees to misuse millions of dollars in Federal funds. In the 7 months since our office was created, we have reported about $40 million in questioned grant expenditures. A sound grants management program is needed, one that complies with Federal requirements and that includes effective monitoring of and assistance to States and other grantees.

Similarly, DHS absorbed billions of dollars in contracts from the component agencies that were awarded under differing procedures and circumstances. DHS must integrate the procurement functions of the legacy agencies, some lacking important management controls. For example, at TSA, where contracts totaled $8.5 billion at the end of 2002, the Department of transportation OIG found that procurements were made in an environment where there was no preexisting infrastructure for overseeing contracts. TSA had to rely extensively on contractors to support its mission, leading to tremendous growth in contract costs. We are continuing to examine these contracts.

Other DHS components also have complex, high cost procurement programs underway that we are or will be examining.

Early attention by DHS to strong systems controls for acquisition and related business processes will be critical, both to ensuring success of the programs and to maintaining integrity and accountability.

With regard to H.R. 2886, OIG has several comments. First, the bill waives the financial statement audit requirement for fiscal year 2003. The amended version offered by the House Subcommittee on Government Efficiency and Financial Management dropped this provision and we support that change. With respect to the proposed requirement for an opinion on DHS's internal controls in fiscal year 2004, the OIG believes such a requirement will be beneficial, but that it is not practical to perform such an audit of internal controls in that year.

The amended version extends the deadline to fiscal year 2005, and OIG supports that change for the reasons outlined in my prepared statement. The amended version also includes a requirement to study the costs and benefits of issuing an opinion on internal controls. We support this requirement as well.

We believe the cost for such an opinion could be substantial—by one estimate, a 35 percent increase in total audit costs. And funds have yet to be provided for even the overall financial statement audit, which we estimate will cost about $11 million, and that is without an opinion on internal controls.

Mr. Chairman, this concludes my remarks. I would be happy to answer any questions you may have.

[The statement of Mr. Berman follows:]

PREPARED STATEMENT OF J. RICHARD BERMAN

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to be here today to discuss financial management and program evaluation at the Department of Homeland Security (DHS).

On March 1,2003, DHS was created by consolidating 22 disparate domestic agencies to better protect the nation against threats to the homeland. In order for DHS to accomplish its multiple missions, it has organized most of these 22 agencies into four major directorates. The Border and Transportation Security Directorate, which maintains the security of our nations' borders and transportation systems, is the largest and consists of several legacy agencies, including the Transportation Security Administration (TSA), the U.S. Customs Service, the Office of Domestic Preparedness (ODP), and law enforcement functions, such as the Border Patrol, of the Immigration and Naturalization Service (INS). The Emergency Preparedness and Response Directorate is primarily the former Federal Emergency and Management Agency (FEMA), and ensures that our nation is able to recover from terrorist attacks and natural disasters.

Smaller agencies were incorporated into the above directorates as well as into the Science and Technology and Information Analysis and Infrastructure Protection Directorates. Additionally, the Coast Guard and Secret Service retained their distinct identities within DHS. The newly created Bureau of Citizenship and Immigration Services will assume the responsibility for immigration services from the former INS. Providing the infrastructure to hold the department together is the Management Directorate, which is responsible for budget, management, and personnel activities.

Each of the component agencies brought to DHS its distinct business processes, which presents DHS with challenges in integrating operations, creating a common infrastructure, and developing goals, objectives and meaningful performance measures to guide and track progress. All of these challenges impact financial management at DHS.

Financial management in the federal government revolves around requirements found in several laws, including the Federal Managers Financial Integrity Act, the Chief Financial Officers Act, the Federal Financial Management Improvement Act (FMFIA), and the Government Performance and Results Act. Agencies must ensure that: (1) government obligations and costs are lawful; (2) funds, property, and other assets are safeguarded; (3) reliable, timely, and useful information is available to make fully informed decisions and to provide accountability; and (4) performance is measured.

Following is an overview of the major financial management challenges facing DHS, along with the steps we believe are needed to address these challenges and establish sound financial management and business processes at DHS. We also provide substantive comments on H.R. 2886, *The Department of Homeland Security Financial Accountability Act,* including the amended version offered by the Subcommittee on Government Efficiency and Financial Management.

OVERVIEW OF FINANCIAL MANAGEMENT CHALLENGES AND SOLUTIONS

Financial Systems and Reporting

DHS must integrate and establish effective controls over the financial systems and operations of the incoming components, many of which bring with them longstanding weaknesses in need of correction. DHS inherited a total of 18 material weaknesses identified in prior year financial statement audits at the legacy agencies. I have included a list and brief description of these weaknesses as an appendix to my statement. We will be assessing these material weaknesses, and the need to retain or add to them, as part of our FY 2003 financial statement audit.

Correcting such weaknesses presents a major challenge. For example, some components, such as INS,[1] have received unqualified audit opinions on their financial statements, but expended tremendous human resources and costs to prepare their financial statements, and weaknesses existed in financial systems and controls. In the past, INS has halted normal business operations for up to two weeks each year in order to conduct manual counts of millions of applications in order to calculate earned revenue figures for its annual financial statements. Poor systems were a major cause of these costly efforts.

While combining the 22 entities and their myriad financial systems and processes pose complex challenges, opportunities abound to achieve greater economy and efficiency. Information systems are a key issue that DHS must address in order to establish sound financial management and business processes. Many of the smaller agencies that came into DHS are still supported by their legacy agency systems and will need to migrate to a DHS platform. The larger agencies brought their own processing capability, but several of these systems have material weaknesses involving system functionality and security. Overall, DHS reports over 80 financial management systems, few of which are integrated.

To meet these challenges, DHS will need to build a unified financial management structure, including integrated and compliant systems as well as consistent policies and procedures. These systems must support not only efficient financial statement preparation; they must provide reliable and timely financial information for managing DHS' current operations, too. A key factor will be the sustained commitment of top DHS leadership, which the Chief Financial Officer (CFO) already has demonstrated. The CFO meets regularly with financial officers and staff from DHS components and legacy agencies that still provide accounting support to discuss the continuing transition and current DHS-wide financial management issues. Further, the

[1] Within DHS, INS has been broken apart and joined with the Bureau of Customs and Border Protection and the Bureau of Immigration and Customs Enforcement. Another part formed the Bureau for Citizenship and Immigration Services.

CFO has formed a group to develop financial system requirements for the agency in coordination with the Office of the Chief Information Officer.

Grants Management

DHS awards over $7 billion annually in grants under its emergency preparedness and disaster assistance grants programs.

DHS absorbed three major emergency preparedness grant programs from FEMA and the Department of Justice (DOJ): the First Responder Program—$3.2 billion; the Assistance to Firefighters Grant Program—$750 million; and the Emergency Management Performance Grant Program—$165 million. DHS also absorbed about $450 million in miscellaneous emergency preparedness grant programs. Previous FEMA and DOJ Office of Inspector General (OIG) reports identified significant shortcomings in the pre-award process, cash management, monitoring, and grant closeout processes. Each of these programs has redundant or similar features such as emergency planning, training, and equipment purchases and upgrades for state and local emergency personnel. Furthermore, program managers need to develop meaningful performance measures related to the degree to which the DHS grant programs have enhanced state and local capabilities to respond to terrorist attacks and natural disasters.

Another complication is that these programs have been divided between two separate DHS directorates. Preparedness for terrorism was placed in the Border and Transportation Security Directorate, while other preparedness efforts are located in the Emergency Preparedness and Response Directorate. This bifurcation creates additional challenges related to interdepartmental coordination, performance accountability, and fiscal accountability. On September 2, however, DHS Secretary Ridge announced that soon he will be sending to Congress a plan centralizing these programs within a single office.

Additionally, DHS absorbed about $2.8 billion in disaster assistance grant programs from FEMA. FEMA's OIG found that it had ineffective performance and financial oversight for these grants, which in turn enabled grant recipients and subgrantees to misuse millions of dollars in federal funds. Grant recipients' problems with financial management, procurement, and sub grant monitoring are long standing. Between 1993 and 2000, for example, auditors questioned the use of funds totaling nearly $900 million dollars. An assessment of mitigation grants awarded between 1989 and 1998 disclosed that half of the $2.6 billion in grant awards was never spent. FEMA's OIG found recurring grant management problems at the state level, too. Often states did not monitor or accurately report on sub grant financial and performance activities. They did not always make payments or close out projects in a timely manner. Their financial status reports to FEMA were often incorrect or past due. And, they did not always maintain adequate documentation supporting their share of disaster costs and other financial requirements. The OIG found that FEMA seldom used its enforcement power to compel grantees to fix problems, even when the grantees had long histories of noncompliance. Finally, the DIG cited FEMA's debris removal program for its susceptibility to serious fraud, waste, and abuse.

A sound grants management program to remedy these concerns must include:

- A comprehensive grants management system that complies with grant financial systems requirements issued by the Joint Financial Management Improvement Program. In addition, DHS must ensure compliance with the Federal Financial Assistance Management Improvement Act of 1999, which requires use of electronic application and reporting by grantees via the Internet.
- Effective monitoring of and assistance to states and other grantees in all phases of the grants management life cycle from award to closeout. Grant closeouts and required audits should be within established time periods, and extensions must be adequately justified, approved, and documented.
- Adequate training and supervision of the grants management workforce.
- Meaningful performance goals and measures of effectiveness.

Contract Management

DHS also absorbed billions of dollars in contracts from the component agencies that were awarded under differing procedures and circumstances. DHS must integrate the procurement functions of several legacy agencies, some lacking important management controls. The General Accounting Office (GAD), for example, reported that Customs had not established process controls for determining whether acquired software products and services satisfied contract requirements before acceptance, nor established related controls for effective and efficient transfer of acquired software products to the support organization responsible for software maintenance. At TSA, where contracts totaled $8.5 billion at the end of calendar year 2002, the Department of Transportation OIG found that procurements were made in an environ-

ment where there was no pre-existing infrastructure for overseeing contracts. TSA had to rely extensively on contractors to support its mission, leading to tremendous growth in contract costs. A review by TSA of one subcontractor involved with hiring airport screeners found that, out of $18 million in expenses, between $6 million and $9 million appeared to be attributed to wasteful and abusive spending practices. Our office is currently reviewing several of the TSA contracts including a detailed audit of the screener contract, in conjunction with the Defense Contract Audit Agency.

Also, some DHS components have large, complex, high-cost procurement programs under way that need to be closely managed. For example, Customs' Automated Commercial Environment project will cost $5 billion, and Coast Guard's Deepwater Capability Replacement Project will cost $17 billion and take more than twenty years to complete. Further, some contracts, regardless of their earlier merits, may need to be revised or may no longer be necessary to accomplish DHS's mission.

Early attention to strong systems and controls for acquisition and related business processes will be critical both to ensuring success and maintaining integrity and accountability. Steps would include:

- Establishing an overall acquisition strategy for modernization of legacy program and financial systems.
- Reviewing all contracts transferring to DHS to ensure they are relevant to the agency's mission and—particularly for systems development contracts—will not be affected by, or conflict with, DHS system integration efforts.
- Ensuring that contracting officers and their representatives are properly warranted, trained, and supervised, and that they maintain proper documentation in contract files.
- Establishing a robust and effective contract management and oversight function.
- Establishing effective systems and controls for managing purchase and travel cards.

Improper Payments

The Improper Payments Information Act of 2002 requires agencies to review all programs and activities they administer annually and identify those that may be susceptible to significant erroneous payments. Where the risk of erroneous payments is significant, agencies are to estimate the annual amount of erroneous payments and report the estimates to the President and Congress with a progress report on actions to reduce erroneous payments.

Since DHS must comply with this Act in FY 2004, we will be performing limited procedures during the FY 2003 financial statement audit to assess the agency's readiness to meet the reporting requirement.

Performance Reporting/Program Analysis and Evaluation

Appropriate plans (including workforce plans), goals, objectives and meaningful performance measures must be established as soon as possible, and is a challenge for any agency. DHS has implemented a comprehensive Measures of Effectiveness project under which such measures will be established through a top-down process based on the DHS strategic goals. We commend the agency for this effort.

Measures of effectiveness are critical to the process of evaluating the degree of success of department programs and operations, and making more informed resource allocations and budget decisions. DIG will use the department's goals, as well as the President's management initiatives, in shaping its own work plans and priorities, and will verify and validate the department's performance data as part of its audits and inspections.

COMMENTS ON H.R. 2886

Presidential Appointment and Senate Confirmation of DHS CFO

H.R. 2886 would amend U.S.C. 31 to include DHS as one of the cabinet level agencies required to have CFOs appointed by the president and confirmed by the Senate. As a result of this amendment, the DHS CFO would also report directly to the Secretary of DHS rather than to the Under Secretary for Management, as is now the case.

The OIG has no position on this change. As a general rule, we believe that making high-level presidential appointees subject to Senate confirmation is conducive to making such an official fully accountable to the Administration and the Congress. On the other hand, the absence of such confirmation does not necessarily mean that the CFO can-not be held accountable. Our primary interest is that the CFO commit to full compliance with the CFO Act, the Federal Financial Management Improve-

ment Act, and all other applicable statutory requirements and general good business practices, and this CFO has done that.

Financial Statement Waiver

H.R. 2886 waived the requirement for a financial statement audit of DHS until FY 2004. The amended version deleted this language, a change that the OIG supported. Completion of a FY 2003 financial statement audit for DHS is important for several reasons. Effective in FY 2004, OMB accelerated the reporting deadlines for Performance and Accountability reports, including audited financial statements, to November 15, 2004. It is unlikely that our office could complete its FY 2004 audit of DHS' financial statements by that date, without at least one year's prior experience, given the short history of DHS and the scale and complexity of its programs and operations. Further, the lack of an audit this year and possible audit timing problems next year could negatively affect GAO's government-wide financial statement audit by increasing the risk of DHS receiving a disclaimer or a qualified opinion.

We believe emphatically that financial accountability for DHS should not be postponed. Its newness, size, and complexity strongly argue for more oversight, not less. GAD has designated the establishment and operation of DHS as a "high-risk" area. An audit of DHS' financial statements is a key oversight mechanism. Not only do audited financial statements provide insight into the reliability of financial reporting, the audit report itself provides details on internal control weaknesses and noncompliance that put financial reporting and safekeeping of assets at risk. We strongly believe that this information should be reported sooner rather than later so that no time is lost in charting and implementing corrective actions.

The CFO of DHS is working diligently to have auditable financial statements for FY 2003 by November 15. Our audit is well underway and we plan to complete the audit by January 31, 2004.

Opinion on Internal Controls over Financial Reporting

H.R. 2886 required that beginning in FY 2004 DHS include in its performance and accountability report an audit opinion on the department's internal controls over its financial reporting. The amended version requires DHS to include management's assertion on internal controls in the FY 2004 report but defers the audit opinion on internal controls until FY 2005.

The OIG believes that a requirement for an opinion on internal controls would be beneficial in concept, but it is not practical to render an opinion on internal controls in FY 2004 for several reasons. Deferral of this requirement to FY 2005 would allow time for the related auditing standards and procedures, and the related costs, to be more properly considered.

Fundamental to rendering an opinion on internal control, under attestation standards currently proposed by the American Institute of Certified Public Accountants (AICPA), is "management's assertion" on controls over financial reporting. Management must provide the auditor an assertion that significant controls over financial reporting exist and are designed and operating effectively during the period under review. In order for management to reasonably make this assertion, it must make an assessment of those controls including an evaluation of control effectiveness using suitable criteria, such as the GAO's *Standards for Internal Control in the Federal Government,* and support the evaluation with sufficient evidence such as testing.Management's assessment of internal controls under the AICPA guidelines would be an extensive, time consuming process requiring sufficient lead time to institute. The need for management to first assess and test controls contributed to a one year deferral of the requirement for publicly held companies to have an independent audit of internal control, pursuant to the Sarbanes-Oxley Act of 2002.

Further, DHS's situation is significantly more complex, with its inception occurring this year, compared to that of a publicly held company that has established processes, financial systems, and the general infrastructure to support the extensive effort required before an audit of internal controls can be performed.

Finally, with the advent of Sarbanes-Oxley, changes are occurring in the auditing profession. Although Sarbanes-Oxley applies only to public companies, it could have an impact on auditing standards for other entities too, including government agencies. The Auditing Standards Board (ASB) of the AICPA in June 2003 submitted to the new Public Company Accounting Oversight Board (PCOAB)[2] its recommended new, significantly expanded attestation standard for reporting on internal control over financial reporting. In the submission letter, the AICP A said it be-

[2] The PCOAB has jurisdiction over auditing standards for public companies covered by Sarbanes-Oxley.

lieved the proposed standard should apply to all engagements and not just to public companies.

It should be noted that the intent behind the requirement to opine on internal controls over financial reporting is similar to the intent behind FMFIA, although FMFIA has involved a far less rigorous process. Consideration should be given to combining these requirements when deliberating the proposed internal control reporting requirements.

Even without an opinion on internal controls, our financial statement audit report will identify material weaknesses and other reportable conditions related to financial reporting. For example, DHS financial statement auditors for FY 2003 will consider internal controls related to financial reporting for grants, procurement, property and equipment, inventory, budgetary reporting, liabilities, and many other categories.

We believe there would be significant additional cost to render an opinion on internal controls. The size of this increment would depend on the extent of evaluation and testing performed by DHS and the audit approach for the financial statements. In the private sector, one survey found that the cost of complying with the internal control reporting requirements of Sarbanes-Oxley would increase the average audit cost by 35 percent. This might be on the low-end for DHS because of its newness and complexity. Further, there will likely be significant costs associated with management's assessment of internal controls, which, as explained above, would be a prerequisite for the audit.

We believe that rendering opinions on internal controls over financial reporting at agencies could be beneficial by identifying additional weaknesses, and focusing attention on the state of financial management in the government. The terminology of a clean opinion versus a qualified opinion or disclaimer provides a ranking system that is easy to grasp. The downside is the additional cost to fund agency preparations and the audit itself.

Study of Potential Costs and Benefits of Audit Opinions on Internal Control

The amended version of H.R. 2886 requires that the CFO Council and the President's Council on Integrity and Efficiency jointly conduct a study of the potential costs and benefits of requiring agencies to obtain audit opinions of internal controls over their financial reporting. We endorse this provision.

We believe the costs, as discussed above, could be substantial. Therefore, it is worth examining the issue to ensure that the most efficient and effective audit procedures can be adopted and that the costs are in line with the benefits. We assume the study will include such an examination.

CONCLUSION

Mr. Chairman, this concludes my prepared statement. I have tried to limit my remarks to the areas of greatest concern and your specific questions. Please be assured that our office will continue to place a high priority on these issues. Again, I appreciate your time and attention and welcome any questions you or members of the Committee might have.

APPENDIX

TO THE STATEMENT OF J. RICHARD BERMAN ASSISTANT INSPECTOR GENERAL FOR AUDITS U.S. DEPARTMENT OF HOMELAND SECURITY

SUMMARY OF MATERIAL WEAKNESSES

RELATED TO FY 2002 FINANCIAL STATEMENT AUDITS

FEDERAL EMERGENCY MANAGEMENT AGENCY

1. Information security controls for FEMA's financial systems environment need improvement.

   Deficiencies existed in the areas of security program planning, training and awareness, background investigations, system certification and accreditation, technical vulnerabilities, terminations, service providers, and wireless communications.

2. FEMA's financial system functionality needs significant improvement.

   Functionality deficiencies included: (1) inadequate accounting functionality in the property management system, (2) inefficient payroll processing, (3) no managerial cost accounting system, (4) interface problems with the HHS' funds disbursement system, and (5) inaccurate vendor table data leading to inefficiencies.

3. FEMA must improve its financial reporting process.
Deficiencies in FEMA's financial reporting process included: (1) significant delays in preparing financial statements, (2) unfinalized standard operating procedures for statement preparation, (3) lack of an integrated financial reporting process, (4) untimely close-outs for interagency agreements, (5) notable adjustments related to de-obligations, expense accruals, and the recording of disbursements as advances, and (6) inconsistent treatment of three unusual contingent appropriations.

4. FEMA must improve its real and personal property system processes.
FEMA lacked a property management system that met its accounting needs. The system only tracked equipment, not other types of property. The system changed acquisition dates for equipment upon transfer and did not link the location of equipment to the accounting records. FEMA did not have procedures to ensure proper property inventories or to ensure the consistent recording of equipment on either a system or component basis. Processes to identify, value, and track construction in progress and deferred maintenance were not fully implemented.

5. FEMA must improve its account reconciliation processes.
Reconciliation deficiencies were noted in the areas of accounts payable, unliquidated obligations, fund balance with Treasury, the suspense fund, reimbursable activity, and intragovernmental balances. Deficiencies were related to timeliness, procedures, documentation, or consistency.

6. FEMA must improve its accounts receivable processes.
FEMA needed to improve its billing timeliness for certain accounts, although it had made progress during the year.

Immigration and Naturalization Service

1. INS' information system controls need improvement.
Deficiencies existed in the areas of access controls, audit trails, back-up procedures, change controls, and system software controls.

2. INS' existing systems are not adequate to record revenue transactions in accordance with federal standards.
The INS did not have a reliable system that could provide regular, timely data on the number and value of immigration applications and petitions received, completed, and pending. This information was necessary to support general ledger entries required for recording fee revenues that were earned when the related applications were completed. Instead, the INS recorded earned revenue in its general ledger when the fees were received.

3. INS' processes for financial accounting and reporting need improvement.
Due to limitations in the design and operation of its legacy financial accounting system, INS did not maintain integrated perpetual general ledger records for many key accrual balances. Instead, the INS used stand-alone systems and performed limited general ledger updates, or it obtained the required balances through manual processes and data calls and recorded "on-top" adjustments as part of the financial statement preparation process. Additionally, the INS did not perform monthly, or at a minimum, quarterly reconciliations of certain major account balances.

Transportation Security Administration

1. Hiring qualified personnel
TSA had not hired sufficient accounting personnel for the Financial Reporting office. At the end of fieldwork, the vacancy rate in the CFO's financial management structure was 50 percent.

2. Financial reporting and systems
Personnel separations from TSA were not processed on a timely basis in the personnel system. Other deficiencies existed in the areas of access controls, security plans, and risk assessments.

3. Property accounting and financial reporting
TSA did not maintain complete and accurate records of its passenger and baggage screening equipment, and an adjustment of approximately $149 million was required to properly record construction in progress.

4. Policies and procedures
TSA did not have written accounting policies and procedures to support TSA's financial management and budgeting functions. Such policies and procedures might have prevented the following deficiencies:

a. An adjustment of approximately $1.0 billion to accrue accounts payable properly for year-end.
b. An approximate backlog of $322 million in purchase orders/obligating documents that were not entered into the accounting system at year-end, often because of incomplete and erroneous accounting information.
c. Adjustments of $309 million and $101 million to correct for improper expensing of equipment meeting TSA's capitalization criteria.
d. Untimely recording of accounts receivable for air carrier and passenger security fees.
e. Lack of a process to develop appropriate disclosure information related to leasing arrangements when initially drafting financial statements.
f. An adjustment of approximately $45 million to correct the expensing of a grant advance payment.
TSA also did not have a process in place to monitor and evaluate its accounting and internal control systems to meet FMFIA reporting requirements.

5. Administration of screener contracts
TSA did not have policies and procedures to provide an effective span of control to monitor contractor costs and performance. Contractors did not always provide evidence to support rates or specific cost and pricing data, nor did they always definitize their contracts, as required. These deficiencies left TSA vulnerable to inflated labor rates and other inappropriate charges.

United States Customs Service

1. Customs did not adequately monitor the effectiveness of its internal controls over the entry duties and taxes in 2002.
After the events of September 11, 2001, Customs suspended its Compliance Management program. This program evaluated Customs' risk-based approach to trade compliance by assessing whether revenue collections reasonably approximated those actually due. Without the CM program, Customs lacked an important internal control related to revenue collection during FY 2002.

2. Drawback controls need to be strengthened.
Customs' Automated Commercial System (ACS) could not perform certain processes that would have facilitated monitoring of the drawback program. To monitor the program, Customs used a risk management process to select claims for review. Although the process was supposed to allow for statistical projection of the results, personnel were allowed to reduce the random sample to a baseline number, thus impeding the statistical projection of results. Reconciliation procedures for related drawback claims also were not sufficiently comprehensive.

3. Customs IT system logical access and software maintenance security controls need improvement.
Deficiencies existed in the areas of network and host-based system configuration, password management practices, logical access controls, application programs, computer-related facilities and equipment, and software patches. These weaknesses put Customs at risk of unauthorized system access, modification, disclosure, loss, or impairment.

4. Core financial systems need to be improved and integrated.
Customs' core financial systems did not provide certain financial information necessary for managing operations. Also, they did not capture all transactions as they occurred during the year, did not record all transactions properly, and were not fully integrated. Additionally, the systems did not always provide for essential controls with respect to override capabilities.As a result, extensive manual procedures and analyses were required to process certain routine transactions and prepare year-end financial statements.

Chairman COX. Thank you. Our next witness is Linda M. Springer, Comptroller of the Office of Federal Financial Management at the Office of Management and Budget. Welcome.

STATEMENT OF LINDA SPRINGER, COMPTROLLER, OFFICE OF FEDERAL FINANCIAL MANAGEMENT, OFFICE OF MANAGEMENT AND BUDGET

Ms. SPRINGER. Thank you, Mr. Chairman. Appreciate the opportunity to appear before you and the Members today to testify on

accounting and financial controls at the Department of Homeland Security.

In the face of many challenges involved with its creation, the Department has demonstrated a very strong commitment to financial excellence and should be recognized for its efforts during this past year. Although the creation of the Department began just 7 months ago, it is off to a good start with regard to its financial management. The Department has shown commitment to preparing audited financial statements in the first year of its existence and to demonstrate accountability to both the Congress and to the American people.

It could have waived, asked for a waiver of that requirement under the Accountability of Tax Dollars Act of 2002, but the Department instead elected to not only prepare statements, but do them on the accelerated time frame to which we are holding other agencies accountable.

This commitment, coupled with the preparation of quarterly financial statements, shows the Department's determination to be fiscally responsible from its inception.

Many issues have been raised regarding the proper accounting treatment of the new Department's financial activity and its presentation in the financial statements that must be addressed. OMB has worked and continues to work with the Department of Homeland Security to resolve these issues in a timely manner.

Undoubtedly there will be new issues that will surface, but we look forward to working with the Department to address them together, in the Department as well. Both the Office of the CFO and the Office of the Inspector General have partnered very effectively with OMB in that regard.

The Department must also begin to address longstanding weaknesses inherited from its components, as you have heard earlier, such as weak financial accounting and reporting processes, inadequate information technology systems, ineffective real and personal property processes and other internal control issues.

The Department has inventoried these weaknesses and is developing corrective action plans. And it will take time, obviously, to implement those, and some of those weaknesses are still in existence.

With regard to performance and information for management purposes, it is necessary for financial managers at the Department to provide management, administration and the Congress with quality, timely information and analysis that better informs about its financial implications of program decisions as well as the impact of those decisions on agency performance goals and objectives.

It is the responsibility of the Department's management to put a process in place that sets performance measures consistent with its strategies, as well as sets goals for achieving its missions and objectives.

You may be familiar with OMB's PART process, that was put into place for the fiscal 2004 budget season, and the PART process attempts to marry up performance measurement with the budget process, and that applies to the Department of Homeland Security as it does for every other agency.

For fiscal 2004, last year's budget process, eight programs at the Department of Homeland Security were PARTed. We have a verb to go with that process. And this year an additional nine programs will be added to the PART process from the Department.

The PART process leads to recommendations that will enhance program performance and will also support GPRA implementation. The PART is a very comprehensive process, and an additional 20 percent of programs in each agency are added each year to the purview of the PART program at OMB.

We believe that this is an important complement to the work that the Department is doing, that the Chief Financial Officer described to you earlier.

With respect to H.R. 2886, there are a few comments that We would offer with respect to the amended version. We are pleased that the amended version does not include the fiscal 2003 requirement for reporting. Obviously, we commend DHS for its recognition of the value associated with going through an audit in its initial year.

With respect to the internal control audit opinion, the amended bill contains a requirement for the Department to have that opinion level audit of internal controls, beginning with fiscal 2005. Additionally the amended bill would also require a study, jointly performed by the CFO Council, the President's Council on Integrity and Efficiency, which is the IG group, and analyzed by GAO.

The administration acknowledges that obtaining an audit opinion on internal controls is potentially useful, yet it is a very significant undertaking. We believe that the insights of a study would be very beneficial across the board, inclusive of the Department of Homeland Security. So we believe that—while we applaud the amendments, we also believe it would be helpful to go further and let the Department benefit from the results of the study in the event that that is not done in time for the 2005 fiscal year.

It is important to note a recent event. You are aware that the SEC had promulgated rules regarding company executives assessing the adequacy of their internal controls. The Public Company Accounting Oversight Board just yesterday met and issued requirements for auditors, the actual audit guidance for assessing these internal controls. So there is clearly a lot of activity in the public—or in the private sector that sets a precedent that we will be considering as we review this requirement, potential requirement.

With regard to the CFO Act piece of H.R. 2886, it is OMB's position that the substantive provisions of the CFO Act should and do apply to the Department of Homeland Security as they do for every other major department and agency of the government. The CFO Act specifies a very specific organizational structure that is inconsistent with the structure that Congress approved when it passed the Homeland Security Act of 2002.

The administration believes that the current construct within the Department is, with a strong and competent leader in two position of Under Secretary for Management, supports not only the CFO office, but provides value in the overall comprehensive view of coordinating not only financial functions but procurement and IT functions. We think that that does add great value, that particular construct.

In every other respect, though, the Department is very much in conformance with the Act from a financial accountability standpoint.

In conclusion, Mr. Chairman, we believe that the Homeland Security Department in its short lifetime has demonstrated a very strong commitment to financial management practices of the highest order, and we have a strong interest, as you do, in preventing potential waste, fraud and abuse, and OMB will be very diligent in working with the Department.

With that, I would close and be happy to take your questions.

[The statement of Ms. Springer follows:]

PREPARED STATEMENT OF THE HONORABLE LINDA M. SPRINGER

Thank you, Mr. Chairman, for the opportunity to appear before you today to testify on accounting and financial controls system at the Department of Homeland Security (DHS).

As you know, the enactment of the Homeland Security Act of 2002 (P.L. 107–296) represents an historic moment of almost unprecedented action by the Federal Government to fundamentally transform how the nation will protect itself from terrorism. Rarely in our country's past has such a large and complex reorganization of government entities occurred with such a singular and urgent purpose.

The government is undertaking a unique effort to transform a distinct group of agencies with multiple missions, values, and cultures into a strong and effective cabinet department. This unique opportunity comes with many challenges, including those related to the new department's stewardship obligation to use tax dollars appropriately and to ensure accountability to the President, the Congress, and the American people. However, with great challenge comes great opportunity-both the opportunity to reengineer and develop seamless systems and processes that support day-to-day operations and the opportunity to provide analysis and insight about the financial implications of program decisions that will ultimately assist this Administration, the Congress, and other decision-makers in evaluating the value and cost of federal programs.

Overview of DHS Financial Management

The creation of the Department of Homeland Security marks one of the largest and most complex mergers ever undertaken by the Federal Government. As with any merger, some of the new Department's efforts must focus on the most immediate challenges. Other efforts, however, by their nature will take several years to successfully develop and implement. For instance, cost control and asset management, coupled with the need to successfully blend individuals from departments and agencies with different cultures, values, and missions, are critical to its effectiveness and efficiency. In the face of the many challenges involved with its creation, DHS has demonstrated a strong commitment to financial excellence and should be recognized for its efforts during the past year. Although the creation of DHS began just seven months ago, it is off to a good start with regard to its financial management.

DHS has shown commitment to preparing audited financial statements in its first year of existence to demonstrate accountability to the Congress and the American people, even though the Accountability of Tax Dollars Act of 2002 allows the Department to request a waiver from this requirement. This commitment, coupled with the preparation of quarterly financial statements, shows the Department's determination to be fiscally responsible from its inception, accounting for all transferred assets, liabilities, and operations. DHS' goal is to obtain an unqualified (clean) opinion for fiscal year 2003 and, if events permit, to issue its performance and accountability report on an accelerated timeframe.

An early challenge DHS must overcome is to obtain a clean audit opinion on its financial statements, which will demonstrate tangible evidence of its efforts to create a premier financial management organization. Reaching that goal, however, will require a cooperative effort among the 22 entities that were transferred to the Department mid-year.

Many issues have been raised regarding the proper accounting treatment of the new Department's financial activity and its presentation in the financial statements that must be addressed. OMB has worked, and continues to work, with DHS to resolve these issues in a timely manner. Undoubtedly, new issues will surface, but we look forward to working with DHS to address them together.

DHS must also begin to address the longstanding weaknesses inherited from its components, such as weak financial accounting and reporting processes, inadequate information technology (IT) systems functionality and security controls, ineffective real and personal property processes, and insufficient internal controls over duties and taxes. The Department has inventoried these weaknesses and developed corrective action plans, although these weaknesses are not yet resolved.

DHS has already taken steps to integrate the diverse financial and performance information systems. It has identified the financial management systems to which the smaller component agencies may migrate beginning October 1. However, this step is just the first of many in a long process to streamline the Department's systems. The Chief Financial Officer (CFO) must also identify the Department's IT assets and then, in conjunction with each program, determine what IT assets are needed to meet mission requirements. The CFO must work with the Chief Information Officer (CIO) to identify a financial management system or systems to meet user needs, whether it be commercial-off-the-shelf, internally developed, or a hybrid of the two.

Establishing Sound Financial Management and Business Processes

The push to create a citizen-centered, results-oriented government has been exacerbated by the demands on available resources. It is necessary for financial managers to provide its management, this Administration, the Congress and other decision-makers with quality, timely information and analysis that better informs about the financial implications of program decisions and the impact of those decisions on agency performance goals and objectives.

It is the responsibility of DHS management to put a process in place that sets performance measures consistent with its strategies, as well as sets goals for achieving its missions and objectives. OMB's PART assessment supplements the Department's performance reviews in the context of the budget process. In addition, DHS management must hold the agency fully accountable in order to attain sound financial management. OMB, along with the Office of the Inspector General (OIG), has the role of overseeing this process. OMB looks forward to continuing to work with the Department to ensure that DHS works to achieve sound financial management practices.

OMB believes that DHS must focus its attention on four critical areas:

- Ensuring top leadership drives the transformation to a single agency, single vision/goal
- Creating the financial organization that adds value and supports the Department's mission
- Establishing seamless financial systems and businesses processes
- Providing meaningful information to decision-makers by routinely generating reliable cost and performance information analysis

Ensuring Top Leadership. Leadership is critical to establishing sound financial management within the Department. The merger of 22 disparate entities into a single financial organization must begin with a clear vision of performance and expectations that is communicated throughout the organization at all levels. To be successful, DHS' top leadership must make attaining that vision a priority, and the message must be reinforced in both words and actions.

Creating the Financial Organization. A premier financial organization must recognize that it exists to provide quality, timely and relevant information about the financial implications of program decisions and the impact of those decisions on agency performance goals and objectives. To accomplish this purpose, leading financial organizations must serve their customers both internally and externally, aligning their mission and organizational structure to better support the entity's mission and objectives. DHS should take all necessary steps toward creating a financial team that supports the overall missions, goals, and objectives of the Department.

Seamless Financial Systems and Business Processes. Building a premier financial organization will also require DHS to establish seamless financial systems and business processes to enable it to successfully fulfill its mission and achieve its goals and objectives. At the earliest opportunity, DHS must determine the essential system and process infrastructure that it requires throughout the organization. This infrastructure must also be flexible enough to support information needs at the detailed program level.

Providing Meaningful Information. In seeking to create a premier financial organization, DHS must also pursue means that will permit it to routinely generate reliable cost and performance information analysis. Such analytics combined with other value-added activities will support the agency's mission and goals. This capability is a requirement for "getting to green" on the *Improved Financial Performance* ini-

tiative of the President's Management Agenda, and it gets to the heart of first-class financial management.

The creation of DHS provides an opportunity to reengineer much of the management reporting formats produced by its components to meet the needs of its users. As DHS looks to develop a new strategic plan that will outline its goals and objectives, its financial organization should design reporting formats that are aligned to measure performance in executing its strategy.

H.R. 2886, ″Department of Homeland Security Financial Accountability Act″

OMB has high expectations of solid financial management practices for this new Department, especially in light of its unique role and function within the Federal Government. To that end, OMB appreciates your consideration of H.R. 2886, the "Department of Homeland Security Financial Accountability Act," and we look forward to discussing several issues of this legislation with you.

Fiscal Year 2003 Financial Reporting and Audit. The original version of H.R. 2886 contained a provision that lifted the requirement of DHS to prepare and submit audited financial statements for any fiscal year before fiscal year 2004. However, much work has been done, and continues to be done, toward the completion of the fiscal year 2003 financial statement process at DHS. Thus, OMB is pleased that the amended H.R. 2886 does not include this provision, and we commend DHS for its recognition of the value that is provided in this initial year by preparing and undergoing an audit of financial statements.

Internal Control Audit Opinion. The amended H.R. 2886 contains a requirement for DHS to "include in each performance and accountability report an audit opinion of the Department's internal controls over its financial reporting," beginning with its fiscal year 2005 report. Additionally, the amended H.R. 2886 would also require that a study regarding the potential costs and benefits of requiring this audit opinion be jointly performed and submitted by the CFO Council (CFOC) and the President's Council on Integrity and Efficiency (PCIE), as well as analyzed by the Comptroller General of the General Accounting Office (GAO).

The Administration acknowledges that obtaining an audit opinion on internal control is a potentially useful, yet very significant, undertaking. While we agree that an opinion level internal control audit could have merit, a review of this magnitude will require the allocation of additional resources and sufficient time to coordinate among agency Chief Financial Officers, Inspectors General, and independent public auditors. Additionally, this provision, if enacted, has the potential of imposing a more stringent requirement on DHS than other Federal departments and agencies.

It is our understanding that this internal control audit opinion requirement is partly intended to hold Federal agencies to the same standards for financial accountability as the private sector. At the present time, however, no other sectors are required to obtain an audit opinion on internal control. While SEC registrants will be subjected in the future to such a requirement under Section 404 of the Sarbanes-Oxley Act (enacted July 2002), the effective date has been delayed as a result of public comments. This deferral recognized several different concerns, which would also apply to federal agencies.

OMB is pleased that the amended version of H.R. 2886 includes a provision requiring a cost benefit study. However, we are concerned that the internal control audit opinion requirement for DHS would take effect with the fiscal year 2005 report, despite any potential determinations by the joint CFOC/PCIE study and the subsequent GAO analysis that such a requirement is not beneficial. Thus, OMB supports delaying the requirement of an internal control audit opinion until after the results of the cost-benefit study can be carefully analyzed.

Applying the CFO Act to DHS. It is OMB's position that the substantive provisions of the CFO Act should apply to the new Department of Homeland Security as they do every other major Department and agency of the Federal Government. However, the CFO Act specifies an organizational structure—direct reporting of the CFO to the agency head—that is inconsistent with the structure Congress endorsed when it passed the Homeland Security Act of 2002. The Homeland Security Act enacted the President's proposal to consolidate management responsibilities at the new Department under the Under Secretary for Management. The Administration believes that with a strong and competent leader in the position of Under Secretary for Management, sound management policies and practices receive maximum standing within the agency.

I hope we can work together to apply the substantive provisions of the CFO Act to the new Department of Homeland Security, while remaining faithful to the President's original proposal to create the new Department, as well as the Homeland Security Act of 2002.

Conclusion

OMB believes that DHS, in its short life, has demonstrated a commitment to sound financial management. Similar to the Committee, OMB has a strong interest in preventing potential waste, fraud, and abuse at DHS and at all federal agencies, and we look forward to working with the Department to ensure that its accounting and financial controls system are as effective and efficient as possible.

Thank you, Mr. Chairman. I look forward to answering your questions.

Chairman COX. Thank you. Our finance witness is Michèle Flournoy, who is a Senior Advisor at the Center for Strategic and International Studies, in the International Security Program. Welcome.

STATEMENT OF MICHÈLE FLOURNOY, SENIOR ADVISER, INTERNATIONAL SECURITY PROGRAM, CENTER FOR STRATEGIC AND INTERNATIONAL STUDIES

Ms. FLOURNOY. Thank you, Mr. Chairman, Mr. Turner, and other members of the committee. Thank you for inviting me to testify this afternoon. I have been asked to address a slightly different issue, as an outsider, the issue of what a strategic planning system might look like for the Department of Homeland Security, based on my own experience in strategy and planning at the Pentagon.

The Department of Homeland Security faces several challenges that really emphasize the need for and importance of strategic planning. Its mission is vital to the welfare of the Nation. It is facing very real day-to-day terrorist threats. It is trying to integrate this very diverse array of organizations with their own cultures and traditions and ways of doing business.

It is responsible for spending billions of taxpayer dollars, and it is trying to balance the very near term with the long term. It needs a unifying vision, a strategy for achieving its objectives, and a clear set of priorities to guide resource allocation and risk management. It is difficult, if not impossible, to do these things absent an effective strategic planning process. So what should that planning process look like?

I think there are five critical elements. The first and what I would call the foundation is a comprehensive and integrated assessment of homeland security threats and vulnerabilities. Such an assessment is absolutely critical to setting priorities, to making the hard choices about where to place emphasis and where to accept or manage risk, to reconciling competing interests and to allocating resources effectively.

The second key element is the development and refinement of the President's homeland security strategy. This is a strategy that should define our national objectives in homeland security, as well as the strategies and capabilities and processes necessary to achieve those objectives. It should clarify an interagency division of labor. It should also clearly articulate priorities for resource allocation across the Nation's portfolio.

Unfortunately, the current iteration of that strategy falls short of meeting these criteria. I believe it needs to be revised. I would urge you to consider tying this document to the budget and performance review cycle and calling on the administration to actually update and submit it to Congress on an annual basis as a foundation for not only the Department's planning, but for interagency planning and homeland security.

The third key element of strategic planning is, as has been mentioned, a 5-year plan for the Department of Homeland Security, and I applaud DHS's efforts in embarking on this exercise. This is something that should provide the Department with a blueprint for developing its budget, identify and prioritize capability shortfalls that need to be addressed, specify short-term actions that deserve to be taken on a priority basis as well as highlight longer term investments that need to be made.

It should be, in my view, an internal classified document that provides front-end authoritative guidance to the various components of the Department for their budget submissions. It should be a living document that is reviewed and revised on an annual basis, though it ideally could form the basis for multi-year appropriations.

The fourth key element is an annual program and budget review process. And, here again, I would applaud the formation of a PA&E office in the Department. This is critical to ensuring that the program and the budget of the Department actually reflects the Secretary's priorities and the President's priorities for homeland security. It is really the key process that ensures that the components are building their budgets according to the Secretary's guidance. It is a key element that allows the Secretary to enforce his vision, his priorities across the rest of the Department.

It is also key to making hard choices, key trade-offs that need to be made early in the budget making progress as opposed to late when it is more difficult to deal with them.

The final key component I would highlight for you is an annual execution or performance review. That is a retrospective look that looks at the Department's previous year of performance and tries to identify where resources were not spent according to plan, flag programs that are no longer a priority, highlight priorities that weren't foreseen before. This is a critical tool for the Secretary to identify key issues for the next program and budget cycle, and to enforce accountability within the Department.

In addition to these elements, there are a lot of intangibles that will be critical to making this a success: Ownership by the Secretary of the process, making sure the process includes all relevant internal and external stakeholders, making sure that there is appropriate interaction across the interagency spectrum.

I think this approach has a number of organizational implications for the new department, and I believe that these could be implemented with a relatively few number of personnel, but would give the Secretary disproportionately large leverage in making these organizational changes. The first is to establish a strategic planning office whose mission expressly is to define and prioritize objectives of the Department and to develop the 5-year plan. This, in my view, should also include a threat assessment unit that is charged with thinking like a terrorist, not dealing with the day-to-day threat assessment but the long term. How is this threat evolving? How do we stay ahead of it as we plan for the future?

The second key element is a Program Analysis and Evaluation Office that is charged with undertaking homeland security mission area assessments and program assessments to identify priorities for resource allocation and to orchestrate the program and budget review process.

The third is an office that is focused on program performance and execution, again an office that would look retrospectively at the previous year's execution and try to enforce a degree of accountability within the Department for upholding the Secretary's priorities.

Finally, as you all consider changes, I would urge you to keep in mind the need for flexibility and adaptability. This is a department that is dealing with a dynamic threat that needs unprecedented flexibility to be able to respond to that threat in a timely manner.

Overall, let me just sum up by saying that I think there is no other department of the Federal Government where a coherent and effective strategic planning process is more important.

Thank you very much.

[The statement of Ms. Flournoy follows:]

PREPARED STATEMENT OF MICHÈLE A. FLOURNOY SENIOR ADVISOR FOR INTERNATIONAL SECURITY CENTER FOR STRATEGIC AND INTERNATIONAL STUDIES

Mr. Chairman, members of the Committee, thank you for inviting me to testify this afternoon before this distinguished body. I have been asked to address the issue of what a strategic planning system for the Department of Homeland Security might look like, based on my strategy and planning experience in the Pentagon.

Although the Department of Defense and the Department of Homeland Security are different in many ways, they do share some common challenges - challenges that underscore the need for and importance of strategic planning in each case. Both are:

- charged with missions that are vital to the health and welfare of the nation—protecting the American people and our way of life is a mission in which we cannot fail;
- facing persistent and resourceful enemies;
- large, complex bureaucracies comprised of a number of diverse and (in some cases, previously independent) organizations with their own cultures, traditions, and ways of doing business;
- responsible for spending billions of taxpayer dollars as efficiently and effectively as possible;
- perennially in the position of having more program than budget; and .
- trying to balance near-term demands against long-term investments.

These challenges make it that much more important for each Department to have a unifying vision, a strategy for achieving its objectives, and a clear set of priorities to guide resource allocation and risk management. It is difficult, if not impossible, to create these absent an effective strategic planning process.

Strategic planning is even more crucial for a brand new department that is bringing together diverse cultures and personnel systems, finding its place in the interagency process, and dealing with very real and immediate threats and operational responsibilities while still trying to get its telephone and computer systems to work. Without a clear strategic planning process, directed from the top, and a cadre of professionals for whom this is their only responsibility, the immediate will always crowd out the long-term planning that is so critical to the Department's ultimate success and to the nation's security.

Strategic Planning in the Department of Homeland Security: Elements of Success

In my view, strategic planning for homeland security must include five critical elements:

- *A comprehensive, integrated assessment of homeland security threats and vulnerabilities:* Such an assessment is critical to setting priorities, reconciling competing interests, and allocating resources effectively. If we try to protect equally against all possible threats, we will protect adequately against none. Although there has been significant discussion of threats and vulnerabilities, no one in government has yet conducted the kind of creative, integrated analysis that is necessary to determine which should be accorded the highest priority - and which should be accorded the least. Without a regular, disciplined, and comprehensive threat and vulnerability assessment process that considers both the probability of various types of attacks and the severity of their consequences, decision makers will have little analytic basis for making tough strategy choices about where to place emphasis,

where to accept or manage a degree of risk, and how best to allocate resources to improve America's security.

• *Development and refinement of the President's Homeland Security Strategy:* This strategy should define our homeland security objectives as well as the strategies, capabilities and processes necessary to achieve those objectives. It should also define a clear division of labor among all of the actors at the federal level, clearly identifying which agencies have lead responsibility in which areas, and which should be prepared to provide support. In short, the strategy should point the way toward well-defined roles and responsibilities, coordination processes, and operational procedures for enhancing the accountability and performance of the U.S. government across the homeland security domain. Based on the integrated threat vulnerability assessment described above, the strategy should also clearly articulate priorities to guide resource allocation for homeland security across the nation's investment portfolio—creating a foundation for unifying the efforts of the federal government and establishing the conditions for effective cooperation and coordination with state and local governments and the private sector. Unfortunately, the administration's current Homeland Security Strategy falls short on a number of these counts and needs to be revised. In order to ensure that it remains a living and relevant document, the Homeland Security Strategy should be tied to the budget and performance review processes and reviewed, updated and submitted to Congress on an annual basis. The Department of Homeland Security should play a critical role in assisting the Office of Homeland Security in drafting this document for the President.

• *Development of a Five-Year Plan for the Department of Homeland Security:* Keying off the integrated threat-vulnerability assessment and the President's Homeland Security Strategy, the Secretary of Homeland Security should develop a five-year plan to guide the Department's activities and investments. Such a plan should clarify the Department's roles and responsibilities in supporting the Homeland Security Strategy, articulate the Department's objectives in its areas of responsibility, and develop strategies for achieving these objectives. It should provide the blueprint for developing the Department's budget, identifying and prioritizing capability shortfalls that need to be addressed, specifying short-term actions to be taken on a priority basis, and highlighting long-term investments to be made to enhance performance in critical areas. This plan should be a classified document issued by the Secretary to provide authoritative front-end planning and programming guidance to the Department's various components in developing their budget submissions. It should also be a living document that is reviewed and revised on an annual basis, though it could ideally form the basis for multi-year appropriations for the Department. The process of developing this plan should include all stakeholders within the Department, as well as close consultations with the White House Office of Homeland Security, relevant Congressional committees like this one, and key state, local and private sector partners. The development of such a strategy-based, integrated, multi-year action plan will be critical to ensuring that the new Department - and the USG more broadly—gets the highest possible return on what is likely to be tens, if not hundreds, of billions of dollars invested in homeland security over the next several years.

• *An Annual Program and Budget Review Process:* In order to ensure that the Department's resources are being spent according to its priorities, the Secretary of Homeland Security should establish a rigorous program and budget review process whereby the activities and expenditures of the Department are reviewed annually in light of the Five-Year Plan's objectives and priorities. This review process would provide a mechanism for ensuring that the actions of various components accord with the Secretary's guidance, and would provide the Secretary with a critical mechanism for monitoring and enforcing implementation of his priorities and those of the President. It also would ensure that the most difficult and important resource decisions and trade-offs come to the Secretary's attention early rather than late in the budgeting process.

• *An Annual Execution Review:* The purpose of this review would be to examine how the Department's monies were actually spent in the previous year, particularly in the Secretary's highest priority areas in the Five-Year Plan, in order to identify areas in which resources were not allocated according to plan. This retrospective exercise is also an opportunity to identify gaps in previous planning, flag programs that are no longer a priority due to changing circumstances, and highlight new opportunities for investment that were not previously foreseen. This is a critical tool for the Secretary to identify issues and lessons learned for next program/budget cycle and to enforce accountability within the Department.

In order to be effective, a strategic planning process for the Department of Homeland Security would require several additional elements. First, it must be "owned" by the Secretary. That is, he must be engaged personally in leading the process and

must communicate to the Department that this is the process he will use to set his priorities and make critical resource allocation decisions. Second, the process must include all internal stakeholders. Any office responsible for implementing an element of the Secretary's Five-Year Plan should be consulted during its formulation. Third, the process must be resource constrained. A strategic planning process that does not take resources into account will fail to help decision makers to make tough choices about where to place emphasis and where to accept or manage risk. In order to be useful and relevant, the strategic planning process must consider the fiscal guidance as a critical input. Fourth, outside stakeholders, ranging from key committees and members of Congress to key partners in state and local government, should be engaged in regular and substantive consultations as the strategic planning process unfolds. Although parts of the Department's Five-Year Plan may need to be classified, the process should not be conducted in secret. DHS will need to create unclassified fora and documents to enable public scrutiny and debate. Your views, as the committee of jurisdiction, should provide critical input to the Secretary as he devises and revises his Five-Year Plan. Finally, the Department's strategic planning effort should obviously take into account broader interagency efforts to enhance homeland security in order to create greater unity of effort across the U.S. government. Ideally, the White House should conduct an annual review of all homeland security programs across the federal government.

Organizational Implications

Putting such a strategic planning process in place would require empowering the Secretary of Homeland Security's office by creating a cadre of 50–75 professionals dedicated to and trained for this function. This small investment of resources would significantly leverage the Secretary's ability to fulfill his mandate.

First, the Secretary's office should include *a strategic planning office* whose mission would be to define and prioritize objectives for the Department and develop the Secretary's Five-Year Plan to meet those objectives. This office would also interact with the White House in the development of the President's Homeland Security Strategy. This office should include a small *threat assessment unit* specifically charged with ″thinking like a terrorist″ and researching likely ways in which the security of the United States could be breached in the future. In contrast to the near-term, operational focus of the more substantial information analysis directorate, this small analytical staff would focus on the mid- to longer- term, and would undertake disciplined reviews of evolving terrorist objectives, doctrine, and techniques in an effort to inform the development of longer-term strategy and investment priorities for the Department. This office should draw widely on the intelligence and research communities in both the United States and other countries.

Second, the Secretary's office should include a *program analysis and evaluation* office charged with undertaking assessments of homeland security mission areas and programs to identify priorities for resource allocation as well as orchestrating the Department's annual program and budget review process. This office could also participate in the annual cross-cutting interagency review of homeland security programs proposed above.

Third, the Secretary's office should include an office responsible for reviewing *program performance or execution* within the Department, as described above. Putting this office under the Chief Financial Officer, who controls the dollars, would likely enhance its effectiveness in being able to hold other parts of the Department accountable and enforce implementation of the Secretary's guidance.

Finally, the administration and Congress should strive to make the new Department as flexible and adaptive as possible. Given the dynamic nature of threats, the homeland security mission will require an ongoing reevaluation of strategy and possibly some rapid changes in programs and resource allocation to respond to new threats that emerge. That is why it is important to make the new Department more adaptive, flexible, and able to work across organizations than those of the past. More specifically, it is imperative that the new Secretary of Homeland Security be given the authorities to reprogram substantial monies in response to new threats, facilitate more rapid acquisition of high priority goods and services, and reform and reorganize offices within the Department with appropriate notice to Congress. This will obviously require an unusually close working relationship with this committee.

Conclusion

Given the importance of its mission, the size of its budget, and the enormity of the challenges it faces, the Department of Homeland Security is in dire need of an effective strategic planning process.Based on lessons learned in the Department of Defense, the relatively minor process and organizational changes recommended here could have a substantial impact on the new Department's effectiveness. Absent such reforms, the Department is unlikely to be able to fulfill its mandate of making

meaningful improvements in our homeland security. Concrete steps should be taken on an urgent basis to empower the Secretary of Homeland Security to establish an effective strategic planning process in the new Department.

Strategic Planning in the Department of Homeland Security

Strategic planning for homeland security must include five critical elements:

- A comprehensive assessment of homeland security threats and vulnerabilities
- Development and refinement of a Homeland Security Strategy
- Development of a Five-Year Plan for the Department of Homeland Security
- An Annual Program and Budget Review Process within DHS
- An Annual Execution Review within DHS

In order to be effective, the strategic planning process must also:

- Be "owned" by the Secretary
- Include all internal stakeholders
- Be resource constrained
- Engage outside stakeholders, such as key members of Congress, in regular and substantive consultations
- Take into account broader interagency efforts to enhance homeland security.

Putting such a strategic planning process in place requires empowering the Secretary of Homeland Security's office. These changes would likely require identifying and training 50–75 people to fulfill these functions—a small investment of resources that would significantly leverage the Secretary's ability to fulfill his mandate.

- Establishing a *strategic planning office* to define and prioritize objectives for the Department and develop the Secretary's Five-Year Plan to meet those objectives. This office would also represent the Department in the drafting of the President's Homeland Security Strategy. It should include a small *threat assessment unit* specifically charged with "thinking like a terrorist" and researching likely ways in which U.S. security could be breached in the future.
- Creating a *program analysis and evaluation* office. This office would undertake its own assessments of mission areas and individual programs as well as orchestrating the Department's annual program and budget review.
- Tasking part of the CFO's office with reviewing *program execution* within the Department on an annual basis to ensure implementation of the Secretary's guidance.
- Giving the Secretary authorities to make the new Department as adaptive and flexible as possible in the face of changing threats and opportunities.

Chairman COX. All of the members except the chairman and the ranking member will be recognized for 8 minutes, who will be recognized for 5 minutes of questions.

Does any Member on our side wish to proceed? Mr. Gibbons.

Mr. GIBBONS. I will yield to Mr. Linder.

Mr. LINDER. I just have one question for Ms. Flournoy. You said something that got my attention, that we should have some group of people in this Department trying to think like terrorists.

If you were thinking like a terrorist, would you be thinking suicide bombings at large events?

Ms. FLOURNOY. I don't think like a terrorist every day. I do think that is something we need to assess. But I am not in a position to give you a credible assessment of likelihood and severity of consequences and so forth.

My point in raising it is I know the Department has a directorate that is responsible for information analysis. But they rightly have a very near-term day-to-day focus and responsibility. I think you need a separate group of people who are focused on the long term and who can inform the strategic thinking of the Department while looking at the long term, and they should be separate from the other directorate and part of the strategic planning organization.

Mr. LINDER. Thank you.

Chairman COX. Mr. Gibbons.

Mr. GIBBONS. Thank you, Mr. Chairman. I had a couple of questions for Dr. Carnes and perhaps Mr. Berman. The view that we

have consolidated 20 plus organizations into one with disparate financial and accounting methods is not uncommon, either in government or in the private sector, especially in the day and age of massive corporate mergers.

Has there been any consultation sought from the private sector with regard to how individuals or entities within this new agency are coping with or dealing with the experiences of mergers of financial accountability?

Mr. CARNES. Yes, sir. A couple of points, if I could. First off, before I came into the administration, I spent 8 years in Defense in the finance and accounting arena, and I was the Deputy Director of DFAS. When I went to DFAS, we had 328 finance and accounting systems in DOD. When I left we were down to 30 systems. We consolidated systems and we consolidated operations.

So I am blessed, I guess you could say, with having had a fair amount of experience in that area myself. I have brought some people in who I knew at DOD who have also been involved in that, and they are applying their skills and knowledge to the problems that we have in consolidation and integration at Homeland Security.

In addition, we have consulted with private sector companies. I will just give you an example. The Hewlett-Packard-Compaq merger, for instance, is one that we recently met with. And they came in and met with the Secretary, and they have briefed the senior leadership on how integration of disparate systems and business processes worked in their case.

I have also visited a number of companies who have engaged in this process, too. So, yes, we do have some familiarity with that.

Mr. GIBBONS. Let me say that in my experience in life change is not inevitable, but the most difficult thing about change is not accepting the new, but letting go of the old way that you have done things. When you change from 22 separate accounting systems to 10, primarily through terminating memorandums of understanding with legacy agencies that are out there, as you report in your testimony, what has been your experience? What comments, what pushback have you received from those individuals who are reluctant to accept changes to their accounting?

Are you able to convince them, cajole them, persuade them in some way to change the accounting methods, even though they are used to the old way that they have done things in the past?

Mr. CARNES. Yes, sir, if you will allow this little anecdote. When I was in DOD, my early years there, we used to try to persuade the military services to change their accounting and finance systems and practices by saying they would be CFO compliant. And I would say to my masters that you show me a CINC who cares about CFO compliance and I will show you a CINC who doesn't deserve his job. His job is to fight war. Our job is to do that as well.

And what we are doing is, we are selling our initiative, because we are going to provide to our operators at the pointy end of the spear the information they need to know and business processes that tell them where they are.

So they are going to get something themselves that is useful here, and they are looking at it. They are involved in the requirements definition process.

Mr. GIBBONS. So this is an incentive basis which you have encouraged them to adopt to the new consolidated procedures of accounting?

Mr. CARNES. Yes, sir.

Mr. GIBBONS. Mr. Berman, of the 80 reports that are out there, financial reports I would imagine, financial management reports, there is an absolute need for consolidation throughout this process. What are you doing to assure Congress that we are getting the right information as reported to us in this process while you look at the consolidation of these various financial management systems so that we have the confidence to know that what is needed for our oversight is actually what is being reported to us?

Mr. BERMAN. Yes, sir. One thing that we have done, similar to what Dr. Carnes was describing, we have in fact adopted a model for the financial statement audit that is used by large, complex corporations.

In order not to miss major issues inherent in the individual components, we actually have six separate teams, each headed by a partner of our CPA firm, that are looking at the underlying systems, controls and accounting processes at those separate components, and then merging all of that information into one consolidated opinion.

This, we believe, will flesh out all of the weaknesses that need to be fixed, including the 18 we have inherited, and possibly some additional ones, so that appropriate attention can be placed on those issues.

I would point out also that for the kind of incentives discussed by Dr. Carnes, we are still talking about the future. The individual components are still largely run using their own systems, which again has largely complicated the audit, and presented some major challenges.

But in the end, I think we will have a comprehensive road map of those issues that need to be addressed.

Mr. GIBBONS. Let me ask a question with regard to the grant system, because out there is an enormous amount of financial aid, financial grants that are being submitted to States at their request. How are we matching up all of the information we are getting back to see whether or not those grants are effective? Are we achieving what we intend to achieve; in other words, a greater measure of security for this country through those grants?

How are you looking at the follow up of those grants?

Mr. BERMAN. We inherited a sizable sum from—in terms of grant programs—from FEMA. And, again, there was—there is quite a history there. We also inherited the entire staff of the IG at FEMA. So, we basically inherited quite a body of knowledge on how those programs are run.

One of the common findings there is the fact that greater attention needed to be placed on overseeing the work of the States. Typically, those grants were made to the States, and the States in turn subgranted to local governments, and that is where a lot of the breakdowns occurred.

We are beginning to focus a lot of our attention on the actual accomplishments of those grants and working with FEMA and the

States to perhaps address some of these systemic problems up front.

One of the areas where we did not inherit a lot of staff is from the Department of Justice. So, one of the first things we did was initiate some work looking at the Office of Justice Programs' mechanisms for awarding and controlling their grants. We are looking into why it has taken so long for ODP to issue grants and for the States and localities to spend the money that they received in 2002.

So, we have a sizable amount of work underway that will help us identify and fix substantive problems in that whole process.

Mr. GIBBONS. Thank you, Mr. Chairman. My time has expired.

Chairman COX. Well, it is good of you to say that for a change. The chairman usually has to point that out.

Mr. Pascrell is next on this side.

Mr. PASCRELL. Thank you, Mr. Chairman. Mr. Chairman, before I get to the questions just an observation, particularly in view of what we are discussing today. All of us up here are, as you are, concerned about developing a Homeland Security Department that is effective as well as being efficient.

But in our hesitancy, excuse me, in our rush to communicate to the American people that we are actually doing something to defend our neighborhoods, I think we should send up a very strong cautionary note about spending.

Because, somehow and in some way, we will jointly defend the Nation at home. But we can't overreact. And I think that is a pretty strong word and I want to use that word. We cannot overreact and simply spend money on what we think we need.

And that leads me to my first question. I was going to ask it to Mr. Carnes, but I would rather ask it first to Ms. Flournoy, and here is the question. Would a comprehensive threat and vulnerability assessment aid the Department's program and budget review process?

Ms. FLOURNOY. I believe, sir, that it would not only aid it, but it is difficult to do an effective strategy development and program review process without it. You know, in the DOD context we always started with a threat assessment. You have to start with an assessment of the environment in which you are working and, make judgments about where you are going to place emphasis, where are you going to accept or manage risk. That is the basis for making choices and strategies, setting priorities, deciding on programs and so forth.

So I think it is exceedingly difficult to undertake that whole strategic planning process without that as a starting point.

Mr. PASCRELL. That is the way it is supposed to work?

Ms. FLOURNOY. That is the way it is supposed to work, and in other departments it does work.

Mr. PASCRELL. We have not included that, though, in this legislation, unless I have missed something, Dr. Carnes.

Mr. CARNES. It is not in the legislation, sir, but we begin with a threat assessment.

Mr. PASCRELL. What do you mean we begin?

Mr. CARNES. When we begin at the Homeland Security Department to do our program and planning, we draw a picture, a threat picture, if you will, with the best information we have available at

the time, to develop that threat assessment so we can guide the development of our programs.

Mr. PASCRELL. Has that been shared with the Government Reform Committee or this committee?

Mr. CARNES. Sir, Mr. Cox referred to—Mr. Turner referred to Mr. Liscouski's testimony. I am not familiar with that testimony. So I don't know what they have provided to the committee. But I can find out for you and get back to you.

Mr. PASCRELL. But I think we would all agree then that in order-before we should spend money—before we have to spend money—there should be this assessment, and it should be very clearly defined so that we are going in a specific direction and we are not spending money before we think or plan. We all agree on that?

Mr. CARNES. As a general matter, I agree with you.

Ms. FLOURNOY. Absolutely.

Mr. PASCRELL. Should this be included in this legislation, do you think?

Mr. CARNES. No, I don't think so because I think that the habits that you are talking about are basic institutional behaviors that DHS is adopting and following. If I might add one point, Ms. Flournoy's comments on what the five key elements are of developing this plan, I could not agree more with her. These are five key elements. We support them and we are doing them.

Mr. PASCRELL. Do we have that, Chairman Cox? The assessment, upon which we are going to base the budget, look at the budget, review the budget, have oversight over this budget?

Mr. CARNES. I was going to say, Mr. Chairman, if I might—pardon me for interrupting—we will publish in the very near future our strategic plan which derives from our assessment of the threat at the time, and that will guide the development of our programming guidance and our budgeting guidance and then our program and budget as it is proposed to the Congress.

Mr. PASCRELL. You know the situation we are in with regard to the budget process. We are heading for the perfect storm and we are looking at, all of us, both sides of the aisle, at what is being spent, and I think we are trying to do that in a respectful and responsible way.

Just a few weeks ago, the Comptroller General of the United States said in a very, what I think is—we all should read the speech he gave before the National Press Club—the Federal Government's current financial statements and annual reports do not give policymakers-I guess that is us-and the American people an adequate picture of our government's overall performance and true financial condition.

Would you agree with that, Dr. Carnes?

Mr. CARNES. Yes.

Mr. PASCRELL. Would you agree with that, Mr. Berman?

Mr. BERMAN. I would.

Mr. PASCRELL. And would you agree with that, Ms. Springer?

Ms. SPRINGER. I would within the context that he was describing it.

Mr. PASCRELL. What about Ms. Flournoy?

Ms. FLOURNOY. I would from a lay person's perspective.

Mr. PASCRELL. This is a pretty serious issue. The recent accountability failures in the private sector served to reinforce the importance of proper accounting and proper reporting practices and I'm very concerned about those practices so that we do not duplicate the error within the private sector, particularly in a new department where we are trying to organize it and we are not clear yet as to what direction it is going in and we are not even clear as to who has oversight over that department.

I mean the fact that something like this has to go to two committees, that it has to go to the Committee on Government Reform and then it has to go to the Homeland Security Committee—and God knows maybe it won't have to go next year because maybe we won't be here—says to me the significance of this committee, which I think is always a question. But one wonders whether we really want to get to the objective, and that is to have a true assessment before we spend the people's money.

Chairman COX. Will the gentleman yield? Obviously Dr. Carnes is not going to comment on our House committee organization but I would point out to the gentleman that the CFO Act has been within the jurisdiction of the Government Reform Committee, which was previously the Government Operations Committee, since its inception, since we originally wrote the legislation. I was very actively involved in that as a member of the committee. And the CFO Act applies to everybody single Cabinet department in the Federal Government. As a result, that committee, the Committee on Government Reform has jurisdiction over its reach to the extent that it applies to all of these different departments and there are always at least two committees, as a result, that will have jurisdiction over this. And it is completely normal that that is the case.

Mr. PASCRELL. Well, Mr. Chairman, if I may.

Chairman COX. As the authorizing committee, we would maintain our jurisdiction over the Homeland Security Act.

Mr. PASCRELL. Chairman, this is the debate we have all the time, and we know who the authorizing committees are. And the problem is that the members—the chairmen and ranking members of all those authorizing committees are on our committee and the question is jurisdiction and I think it is a very valid question as to whether we want to move forward or whether we want to get stuck in the bureaucracy. We need answers and we need action. That is why I asked the question. That is why I brought emphasis to the point.

Thank you.

Chairman COX. The gentleman makes a very good point, and I think as you know our Rules Subcommittee is working diligently on this. My own view, and I think the view of most of the members of this committee, is that it is vitally important that there be one authorizer for this department if we are going to have success, if we are as a Congress going to participate in an effort that is going to be successful.

Mr. Sweeney is recognized for 8 minutes.

Mr. SWEENEY. Thank you, Mr. Chairman. I am probably not going to take the full 8 minutes. I have some simple questions and really a statement, and it is consistent with some of the questions that have been asked. Certainly, I think it is consistent with what

Mr. Pascrell was just talking about, but it is a perspective that I don't think has been stated by too many Members of Congress.

All of you have given testimony that—and all of you have endorsed the notion of establishing a process of developing better strategic planning or some strategic planning in this instance. But haven't we in Congress set you up for a fall? And that is from my point of view we have established a system of formulization throughout ODP grants and the grant process that is fundamentally so flawed you cannot do strategic planning because you are locked into some arbitrary formulizations that from where I come from do not make a lot of sense. They are counterintuitive or counterproductive to the idea that we establish a stream of funding that is threat-based. We sort of treated it like Congress kind of treats everything, and that is, "I have got to make sure I bring something home."

And so this committee I think is going to, in a broad bill, address some of the formulization issues. I have a bill of my own that bases the ODP portion—and I hope it serves as a precedent—on threat, vulnerability and consequences and, therefore, I think directs from Congress to the agency itself the kind of focus that you need to be able to create the strategic planning and the management style that you need.

I would like to hear from Mr. Carnes and Mr. Berman on this. And then I want to talk about the back end of it because I think what we need to do is give you the tools to be able to focus the dollars where they need to go and then we need to be assured—I agree, Ms. Flournoy, that there needs to be flexibility here, but we need to have the confidence that within that flexibility we are going to be able to quantify the results.

Dr. Carnes, please tell me how much an impediment is the current formulization process?

Mr. CARNES. The Secretary in the fiscal year 2004 appropriations process talked about this issue at great length in a variety of different forums, and I will just say that we are very pleased in the way the appropriation came out with the flexibilities that we can get in the ODP grants because those flexibilities do provide some discretion to respond to where we see an increased threat and vulnerability and risk.

Mr. SWEENEY. If I could interrupt, if there is a requirement that you send 40 percent based on some per capita notion, seemingly grabbed out of the sky in our rush to make sure we get something established, which is understandable, how effective can you be at getting dollars to where real risk exists and how flexible can you be to adjust that? I don't see how it works.

Mr. CARNES. I guess I would answer it this way. Obviously, in a world—in one kind of world you would have complete flexibility to deploy your assets as you deem appropriate. There are, however, other concerns that those involved in this process have and bring to bear, and that is what gets enacted.

Mr. SWEENEY. We cannot get it passed—I understand, we can't pass it unless someone feels like they are bringing something together. Is it an impediment? Rate it: High, medium, low.

Mr. CARNES. I think I am going to leave that to the Secretary. Thank you, Mr. Sweeney.

Mr. SWEENEY. Well, Dr. Carnes, how are not going to answer that if you are the person in the position best able to offer us that advice? I am trying to help you here.

Mr. CARNES. I am going to say at least medium.

Mr. SWEENEY. Mr. Berman?

Mr. BERMAN. First of all, I would agree with Dr. Carnes' characterization as medium. Our office certainly endorses and would endorse any move to apply some sort of threat analysis before distributing those funds.

One of the things we found in our recent assessments, interestingly enough, is that one of the reasons why it has taken some States and localities so long to spend the money they received in 2002 is that they are really trying to do it right. They have slowed down the process, in some cases, in order to try to make the equipment being purchased at the local level interoperable and to ensure that local plans are somehow integrated with State plans. This is not necessarily across the board, but we have seen a lot of that discipline at the State level already, and we are encouraged to see that.

But again, I think in the final analysis there deserves to be a heavy emphasis on risk assessment.

Mr. SWEENEY. Right. The other two witnesses want to comment at all? Okay. Let me ask this question as a follow-up.

I believe we have to restructure the methodology to get the funds out. But then we need to have the confidence that once that happens, we have tangible and appropriate measurements. So what are the metrics that would be needed to be developed in an audit process and how confident should we be that this mega agency now would be able to develop it so it could be implemented agency-wide?

DOD—Ms. Flournoy, I agree with everything that you said, except DOD has had problems with its own audit processes. So maybe we could have that discussion about the audit metrics.

Mr. BERMAN. I think the basic thrust of the IG's work is to assure that funds are invested wisely and that those investments produce measurable improvements in security.

Which is where risk-based assessment comes in. First, there needs to be an agreement as to what is it exactly we are trying to accomplish with those grants? What are we trying to protect? What is the baseline today and how much do we expect that baseline to improve based on the investments we make?

Mr. SWEENEY. Dr. Carnes, have your offices begun that kind of focused attention and developed that kind of product?

Mr. CARNES. Yes. Yes, we have. I have got right here, this is a draft list of performance metrics that we are going to—we are running through a clearance process in the Department right now that will accompany the budget when it comes up. This will be the grade card. When we do our budget review, the thing we want to know is what is the thing you are buying, why are you buying it, and what are we getting for it?

Now, those are—your question was a great question because those are rock bottom, the very toughest issues to decide. I am not so much interested in process as I am in product. I want to know what the thing is. But the real trick is to figure out does it make

a difference? That is a very tough one to assess. Is that the thing that prevents terrorism? How do you know? That requires good intel. You have to know where to aim.

Mr. SWEENEY. As I see my time has run out, let me give you a little bit of advice. The more interactive you are with this committee in particular, but with Congress in general on the establishment of those metrics, the more successful you are going to be. And believe me, we all want you to be very successful. Thank you.

My time has expired, Mr. Chairman.

Chairman COX. Dr. Christensen is recognized.

Mrs. CHRISTENSEN. Thank you. Mr. Chairman, I do not have any questions at this time.

Chairman COX. Mr. Langevin is recognized.

Mr. LANGEVIN. Thank you, Mr. Chairman. If I could just follow up on a question Mr. Pascrell touched on and the previous question also for Mr. Carnes. In your testimony, you said that DHS has initiated a 5-year budget and planning program, and I am certainly pleased to hear that. But I am curious to know a little bit more about how this plan is being developed, whose input you are seeking in setting it up. Specifically, I want to know if the Information Analysis and Infrastructure Protection Directorate has had any role in this planning process and what information you are basing that plan on, given the fact that DHS has really yet to develop a comprehensive threat and vulnerability assessment, because it seems to me that this is obviously a critical precursor to a significant long-term budget decision. Likewise, how is your programming and budgeting system being developed in the absence of an overarching set of goals and priorities based on threats and vulnerabilities? I certainly appreciate the fact that you are seeking to follow DOD's successful program, but as you know, DOD already has in place comprehensive multi-year strategic plans, the QDR, Quadrennial Defense Review Plan and others that are continually updated and used throughout the Department as a reliable statement of priorities. So if you could elaborate on that, I would appreciate it.

Mr. CARNES. Thank you for that question. It is a big question. We were going to do, when we went over to Homeland Security, a 5-year program and planning exercise whether it was required by law or not and we were pleased to see that it was required by law and that it referenced the DOD model in statute as the one that we should follow.

The first year, in developing our fiscal year 2005 budget proposals, obviously we started in the spring and had to do lots of things simultaneously that normally we would do sequentially. We took our guidance from the President's National Strategy for Homeland Security. The Secretary issued guidance based on the President's strategy and his refinements of that strategy and issued guidance to the components to develop budget proposals in response to that. In the meantime—to that guidance. In the meantime, we began the development of our strategy and our POM process to lead to the 5-year program. So all of these are going simultaneously, as I say. Beginning with the next one we do, these will all be sequential and one will flow to the next and one drives the next.

But we do not, absent—we do not have information on which to build a program. What we are talking about now is the refinement and a fine-tuning, a calibration of the strategic plan and of the program guidance to implement that strategic plan. But the principles that guided our program and budget for 2005 and the 2004 budget that was just passed were pretty clear principles and laid out very directly and succinctly, and those are what guided our program and what are guiding our program now.

As to a threat picture, yes, we do have to have a threat picture. Is IAIP at the state that it wants to be? I don't think that it is. It is still evolving but that does not mean it is not doing anything. It is doing quite a lot of intel work. Quite a lot of threat assessment. And it is lashed up in the TTIC with FBI and CIA. And the Intelligence Community, working together, is providing this threat picture. That is what shapes our programmatic response.

Mr. LANGEVIN. So how are IAIP and others—.

Mr. CARNES. We are doing what we call an environmental scan before we issue what the programming guidance would be, and the IAIP is the source of that information. They are the ones who inform the process with a threat picture.

Mr. LANGEVIN. And then they and others are communicating that and that is the way you are going to form a comprehensive 5-year plan?

Mr. CARNES. Every major component in the Department is a major player in the development of a 5-year plan. When we have a threat picture and when we refine the threat picture, then programmatically we develop guidance that the Secretary sends out to respond to that threat, to address that threat. The programs then develop their program proposals which come in and get reviewed by the senior officers of the Department. That leads to budget guidance. That goes to a budget review board of all senior officers of the Department trading off this against that and then in responding coherently to the whole thing, to the whole threat.

So we try to make our decisions corporately as a corporation of senior leaders in the Department, but wearing two hats if you will. They are also proponents for their own particular organizations, but they are asked to make corporate decisions. The guidance comes from on top, the response comes from below. It filters up to the top and then the programmatic response is adjusted to fit that threat.

Mr. LANGEVIN. Now, have you brought in consultants that help the DOD prepare its QDR to help you in this planning process as well? Not consultants, but people from DOD?

Mr. CARNES. Oh, yes, this guy right here I stole from Energy and previously they stole him from DOD. He is Dick Williams, the head of PA&E for me, and he has a long experience in program analysis and evaluation and he is doing a first rate job. And he has brought on his staff people from DOD and we have people throughout the organization with a DOD background.

Mr. LANGEVIN. I hope to follow up on this further.

If I still have time, Mr. Berman, I appreciate your comments about the need for a grants management program and I certainly agree wholeheartedly. I was, though, very surprised to find recently that there is not even a simple database in place to track the

money that flows to each State from DHS. My staff recently called the Department to find out more information just, for example, about a DHS grant being announced in Rhode Island which we had not received any notice of. And there was apparently no easy way for DHS to look up the list of grants that Rhode Island had received. Instead we had to speak to at least three different legislative liaisons in separate offices before we could even take an educated guess as to where the money was coming from.

Let me say for the record that the staff there was very helpful, but I just found it amazing that no comprehensive database exists in order to help them access such basic information.

So my question is would you comment on that and would your grants management program offer solutions to this problem?

Mr. BERMAN. Absolutely. We have the same frustrations with the lack of such a system and we rely heavily on our—at least three of our regional offices to track the grants going into those areas. But certainly such a system would be at the heart of any system that would allow DHS to manage the flow of those grants and the status of those grants.

We are somewhat hopeful with some of the developments at ODP—or what was ODP—in developing Internet-based systems to make it at least easier for applicants to request grants and then subsequently to track those. But we are still a long way away from the system that you are describing.

Mr. LANGEVIN. My time has expired. Thank you.

Chairman COX. I thank the gentleman. The chairman recognizes himself for purposes of questions.

Dr. Carnes, my understanding is that the Department expects to have auditable fiscal year 2003 financial statements by November 15th?

Mr. CARNES. Yes, sir.

Chairman COX. And you are on track to have an audit completed in January; is that right?

Mr. BERMAN. That is correct, sir.

Chairman COX. January 31st?

Mr. BERMAN. That is correct.

Chairman COX. Do you expect, Dr. Carnes, that that will be accompanied with a clean opinion?

Mr. CARNES. Yes, I expect that it will. There are a couple of hurdles we have got to get over and I think we are going to get over them, but I think we will get a clean opinion.

Chairman COX. You were clear in your testimony, I believe, that it is the view of the Department that the CFO should not report to the Secretary and not be confirmed by the Senate; I am correct?

Mr. CARNES. Yes, sir.

Chairman COX. And that is OMB's view as well?

Ms. SPRINGER. Yes, it is.

Chairman COX. Mr. Berman, you stated that OIG has no position on this change?

Mr. BERMAN. That is correct. We have certainly seen it work both ways. Our primary concern is that the Department does, in fact, follow all of the requirements that fall under the CFO Act, and the Department, and Dr. Carnes has pledged to do that.

Chairman COX. Ms. Flournoy, you worked at DOD. At the Department of Defense, the CFO reports to the Secretary; is that correct?

Ms. FLOURNOY. Yes, and it requires Senate confirmation.

Chairman COX. Did that work in your view?

Ms. FLOURNOY. It did.

Chairman COX. Is there a reason that you can imagine that DHS should be unique among Cabinet level agencies and not have that requirement apply to it?

Ms. FLOURNOY. Sir, I am not expert in that area so I really can't offer you a judgment.

Chairman COX. I am going to give Ms. Springer an opportunity to convince me that DHS should be the unique cabinet department in this case.

Ms. SPRINGER. I don't know if I will be convincing to you, Mr. Chairman, but I will give you a few points of information that may be helpful.

My observation since I have been here over the past year is that while the act does require the reporting line to be drawn between the CFO and the Secretary, that in practice most of those CFOs are working connected to either the Deputy or some other Under Secretary, for Management in some cases.

Chairman COX. In fact that is right and that reporting requirement is as much an imposition of responsibility on the Secretary as it is a guarantee of a reporting line to the CFO.

Ms. SPRINGER. Right. And so I think that what has motivated that is to make sure that the Secretary is well plugged into financial accountability issues, that he or she takes them seriously.

Chairman COX. So in a word that the Secretary is accountable?

Ms. SPRINGER. Right. And I think that what we have found at the Department in our observation of Dr. Carnes and his interaction with Secretary Ridge and that there is that continuity or connection, that the Under Secretary facilitates that in this case, that the Under Secretary actually is able to coordinate the message that gets to the Secretary so he receives it in its fullest context.

So its relationship to IT and procurement and other financial issues—.

Chairman COX. Given the way the other agencies are functioning under the CFO Act, is there any reason to think that that could occur in DHS in the way that you are describing?

Ms. SPRINGER. It could occur. We have seen the product coming out of the Department on par and with the same seriousness that we see in other areas. I would say it both could work but it was more a sense of the coordination that this structure would provide.

Chairman COX. Dr. Carnes, are you planning to use outside auditors for any purposes?

Mr. CARNES. The IG is using outside auditors in auditing our financial statements as well as doing some of the work with his own folks. I could conceivably—I can envision a circumstance in which I would hire a team from such an outfit to come in and look at an issue that I was concerned about if I did not have the staff to be able to do it.

Chairman COX. Mr. Berman, do you want to describe your plans in this regard?

Mr. BERMAN. Yes, sir. Again, Dr. Carnes is correct. We are using a firm—we have engaged a firm to do both the audit—

Chairman COX. Which firm is that?

Mr. BERMAN. KPMG. They have been engaged to do the audit for both 2003 and 2004 since in effect you almost need to start planning 2004 because of the accelerated time frames.

Chairman COX. Can you describe the scope of the engagement? What are their responsibilities in connection with the audit?

Mr. BERMAN. They are responsible for arriving at an opinion on the financial statements presented as a whole. I would also clarify for the record OIG's position on the issue that you addressed with Dr. Carnes regarding a clean opinion. I appreciate Dr. Carnes' optimism that we will have a clean opinion. I think from the IG's standpoint we see the road ahead a little bit steeper than that. The obstacles are quite formidable and I would not want people to at this point expect a clean opinion. It will be a real challenge.

Chairman COX. Apart from the significant work involved in KPMG's engagement to audit the Department's financial statements, have we asked KPMG or any other outside firm to consult on the subject of the consolidation of financial controls within the Department with the 22 legacy agencies?

Mr. BERMAN. One of the reasons that we chose KPMG, and in fact this case we went sole source for those 2 years because KPMG has already done substantive audit work at many, if not most, of the big components and we felt that KPMG could bring to the process a depth of knowledge about the specific operations of those individual components that we could not gain anywhere else.

So now KPMG itself essentially is relying on its own staff in areas where perhaps some other IGs—or other CPA firms might bring in additional experts, such as in the area of penetration tests. They are using their own specialized staff, for example, to attempt to penetrate some of the financial systems or the networks that those systems are connected to. So essentially at this point we are relying primarily on KPMG.

Chairman COX. My specific question was are we asking them, in addition to their audit work, or are we asking any other firm, to offer assistance to the design of financial controls in the Department of Homeland Security, which after all is a merge of 22 legacy agencies?

Mr. BERMAN. At this point, no, sir.

Mr. CARNES. Actually, sir, that is my job and we have met with many of the firms already, and they have wasted no time in actually coming to see me because they know that is the business that we are going to be in. And we on our staff had a lot of familiarity with these firms, having worked with them on these kinds of projects in the past. We will be offering an RFP for contractor support and it will be substantial. We will probably have 350 people involved in this initiative, most who will be contractors or subcontractors from one of the major firms. Probably one of the major firms, but anyway whoever does the best job in the contract. But we will be having a lot of outside support.

Chairman COX. And this RFP that you have in mind is going to cover what?

Mr. CARNES. It is going to cover the integration of finance, accounting, and budget systems across the Department and procurement systems, and it is going to develop the plan for integrating them and then deploying the solution within 2 to 3 years.

Chairman COX. And when do you expect to issue your RFP?

Mr. CARNES. In the late winter, early spring. We are engaged in a requirements definition process working with the components of the Department.

Chairman COX. Is it going to be the aim of that undertaking to redesign the financial controls of the Department?

Mr. CARNES. We are not going to throw out anything that works but anything that does not work we are going to shoot in the head and redesign it.

Chairman COX. One of the things that I admire about your background is that before you entered government service you were an English professor and we need such people in this business who can speak English. But I want to be very clear what we are talking about here. We have got 22 separate agencies all with their legacy systems, 18 material weaknesses identified in the most recent audits. A lot of problems. And a great opportunity—

Mr. CARNES. Right.

Chairman COX.—to throw out all the trash and do it right in a way that works for homeland security, which in fairness to all of these agencies was not even their design in the first place.

Mr. CARNES. Right. Right.

Chairman COX. That is an ambitious opportunity but it is a great opportunity. And my question is, is that what we are doing? And is that work that is going to commence essentially with the issuance of this RFP next spring?

Mr. CARNES. Basically, that is what we are doing. We will shrink the number of systems way down. We will have solid internal controls. It will be JFMIP compliant and it will be instantaneous real-time information for our managers, decision makers and operators, and we will strangle things that are not working.

Chairman COX. How do we—when we hire a firm to do this, how do we ensure that this is not just a financial exercise? Let's take the One Face at the Border initiative of the Department. we are putting together APHIS and Customs and INS, each of which has separate accounting systems. The way that you pick and choose among those or redesign them has a great deal of influence on the way people do their work. If we pick the INS approach as opposed to the Customs approach, that probably makes people at Customs unhappy. How do we make sure we are infusing management objectives into this process?

Mr. CARNES. That is the essence of the requirements definition process. We are going to meet—the people who are involved here are not just or even financial geeks. We want operators who are folks—you cannot manage an organization with a financial statement, in response to somebody's question a moment ago. You cannot run an organization that way. You have to be accountable and produce the financial statements so that people know what you did with your money, but you cannot run an organization that way.

You have to have a financial system that has the capability of giving you meaningful information. The essence of that is the in-

volvement of our senior people throughout the Department. It is our expectation that the Secretary will shortly launch that initiative and call upon them to be involved from the get go.

Chairman COX. On the subject of getting useful management control information, let me dive immediately into what we learned about INS at the end of last year.

The INS, which Congress abolished and is no more and is reconstituted within DHS in two principal parts, was on the way in the door unable to provide data on the number of immigration applications it received. It could not tell us how many of those applications were a work in process and how many of those applications were complete. This showed up in an audit because there are fees that are paid in conjunction with this, and in a flourish of Enron style accounting the Federal Government was booking the revenue before it did the work and then lost track of the work as a result.

The proper way to do this, it is my understanding, is to book the fee as revenue to the government when you process the application and not before. This is something that has been identified as a problem. But it is not just a financial problem, it is a Homeland Security problem because if we cannot track our work flow, there are human beings behind these applications and they are the human beings that we are interested in putting into our watch lists and tracking in a U.S. visit program and in all other aspects.

So the breakdown of a system that is supposed to keep track of the most basic thing, which is I applied, I have an immigration application and petition, I sent you a check, and we do not even know those figures that is pretty frightening, isn't it?

Mr. BERMAN. Yes, sir, you are absolutely correct in your description of that problem. We are hopeful that the problem will be fixed this year.

The DHS has implemented, the component (CIS) has implemented, a new system which is now being tested. To the extent that the system has been operating this year, we are comparing the results in that system to the actual results in selected offices. And hopefully, that will get us over this problem.

Chairman COX. I am sorry; I was just having someone whisper in my ear and I missed your last sentence.

Mr. BERMAN. If those tests are successful which the auditors are conducting now—comparing the actual applications in selected offices with what the numbers are in the new system that they have developed—hopefully we will be over this particular problem. But this has yet to be seen. Those tests are still under way.

Chairman COX. We got the same bleak report when it came to grants. The amount of money that was missing was rather significant over the period between 1993 and 2000 and grant programs that are now the responsibility of DHA. $900 million just went missing.

Mr. BERMAN. Sir, it is not that the funds were missing, but basically what happens is these grants are related to particular disasters. For some of these disasters, like the Northridge earthquake, there is still an office, a FEMA office on the West Coast, trying to resolve those issues almost a decade after the actual event. Unfortunately, what happens is some of these individual grants do not get closed out until years after the event. When the auditors arrive,

they find that some of the funds were not spent in accordance with the actual grant agreement, and that is what results in much of those questioned costs.

Chairman COX. In fact, the $900 million to which you refer in your testimony and to which I just referred as well is not money that went missing. That is money that was spent for questionable purposes?

Mr. BERMAN. That is correct, sir.

Chairman COX. But there was another $2.6 billion, half of which was not apparently spent at all, and that is the money that in my mind is missing. What is happening to money that is not spent? It is granted, but it is not spent?

Mr. BERMAN. Yes, sir, this is basically no-year money. And, the reasons are quite varied. In some cases, the States and/or the localities simply are slow to develop specific plans to meet the State's requirements.

Chairman COX. No-year money is the same accounting device that we used this year when we created the BioShield program. And my understanding of this accounting and this legal authority that we are granting in this fashion is that it is indefinite so it mimics a permanent indefinite appropriation. Are you telling me that there is money that is out there from 1993 and we are going to get a drawdown on that at some point?

Mr. BERMAN. Yes. As far as the money that was cited by the former FEMA IG, I don't know the exact status of that. I am hopeful that by this time the bulk of that, if not all of that money has been spent.

On the other hand—.

Chairman COX. I am not sure. If the grant was made way back then and people are just coming up with a reason to spend it now, maybe it would be best to jump in with legislation and take that money back.

Mr. BERMAN. Sir, we are currently looking at the money that was awarded by ODP in 2002 to get a more recent understanding of how that money is being spent. And similarly, we found most of that money has not actually been spent. Now, a lot may have been obligated, but as much as 90 percent may still be unspent.

Chairman COX. I had intended to go last and wait until all the other members asked their questions, but I know that Ms. Jackson-Lee was here and wishes to ask questions. Mr. Shadegg, I don't know if you wished to ask questions, so I will yield to my colleagues.

Ms. JACKSON-LEE. Thank you, Mr. Chairman. I will not have time to ask my questions, but I simply would like to indicate that my interest is to ensure that there is fiscal accountability, and as well I have always been concerned about ensuring that grants that are rendered by the Department have the opportunity to be directly rendered or given to local communities. The process that you have now is that it is directed through the States. And so any time we have that opportunity to refine that, I know that may be legislative, but I would hope that we would be able to take that into consideration in terms of the funding. Right now the funding is through the States and I believe that is a delaying tactic that is not warranted.

Ms. Flournoy, I think you have talked about threat assessment and the necessity of that. Do you have a quick response as to the need for having a strategy—Homeland Security strategy that would then direct the CFO as to how to budget priorities? If you could just give me a quick answer on that.

Ms. FLOURNOY. Sure. I think developing a comprehensive strategy is one of the critical elements of a strategic planning process. I think it needs to happen at the interagency level, signed by the President, and then within the Department of Homeland Security they need to develop their own strategy in concert with the President's strategy to go forward.

Ms. JACKSON-LEE. Would that also include local communities and States as well, that they do a far-reaching effort in terms of input?

Ms. FLOURNOY. The focus of the strategy would probably be on how the Department is going to use its resources. But to be effective they would have to include representatives from local and State government and communities as stakeholders in helping them define their vision.

Ms. JACKSON-LEE. Thank you for your leadership. I yield back.

I ask unanimous consent to put my statement in the record.

Chairman COX. Without objection.

The gentleman from Arizona is recognized.

Mr. SHADEGG. Thank you, Mr. Chairman. I want to begin, Ms. Flournoy, by thanking you. I thank all the witnesses for your testimony and for your efforts on behalf of the Department. I particularly want to say, Ms. Flournoy, that I agree with you and your testimony on the importance of threat-based or vulnerability-based assessment. It seems to me any other prioritization of the agency's resources or of our Nation's resources to protect us against a terrorist attack, other than one based on threat, is a mistake. When we do it based on population or based on some other type of formula, I think we are making a mistake. And this is my own personal bias.

I strongly believe that the American people expect us to be very forward-looking in our approach to homeland security. And by that, I mean that I think they want us to be looking at the threat before it occurs, doing all of the intelligence we can, all of the assessment and evaluation we can, and everything humanly possible to preclude those attacks before they occur. Now, that is not to diminish the importance of first responders. God forbid a future attack is successful in inflicting harm on Americans on American soil. But I think the Department's focus has to be very aggressively on reaching out and looking at where is it that we are threatened? Where is the next attack going to come from, where are we vulnerable, and how can we prevent that attack if that is at all possible. So I encourage you for that testimony and strongly concur in it.

I want to turn next to Ms. Springer. You put out, I guess, a report OMB does each year called performance and management assessments. I want to ask a couple of questions out of the section of that report on Homeland Security. Apparently what you do is you go through program by program. This particular program that caught my attention is Disaster Relief Fund Public Assistance. As I understand the format, you evaluate the purpose of the program, its purpose, its management, its results and accountability. On

page 43, if you happen to have this report, you say that the purpose is very high. You rate that as a 90. But then you say the results and accountability are very low. And you say for example: "The program"—now this is the disaster relief fund which goes in after a hurricane—"the program has no long-term outcome measures, it cannot meaningfully track operations with annual performance measures and the program fails to adequately screen requests for assistance to determine whether Federal help is needed."

On a program as important as disaster relief, I think that is a very, very telling analysis. And you come back and say rating results not demonstrated, meaning they have not demonstrated results from their program. The question I want to ask is not specifically about that but as a general proposition, doing this year over year, do you see departments then improve programs of this type? Can we expect that as a result of this evaluation, the Disaster Relief Fund Public Assistance Program will improve and have you had discussions on that topic with DHS?

Ms. SPRINGER. Okay. It is an excellent set of questions. Let me just first say there is someone at OMB who is charged with overseeing this Budget and Performance Integration Initiative. It is one of the President's management initiatives that all the agencies are rated on. I am not that person, but—so I will provide you with what information I do have and would be glad to give you a more detailed answer.

That program was one of eight programs that was measured last year. The whole process of evaluating those programs had its inaugural year with that fiscal 2004 budget process and the objective was that in rating it, not only the purpose but its effectiveness and its results and accountability and all the things that you mentioned, would continue from year to year, with that being the first year. It will be reviewed again in this year's process as well as another nine programs that will be added and we will look for improvement obviously.

The theory behind this whole process is that if the results are not demonstrated, it may mean that there is more funding required to get it to that threshold. On the other hand, it may mean that the funding is not being properly utilized. There are a number of conclusions you can draw and it will be reviewed again each year after that first inaugural baseline year where the results were not demonstrated. And we found that in a number of programs, but this process complements and supplements what the Department is doing itself.

Mr. SHADEGG. I want to ask the Department about that in a moment. This is a flyer explaining that FEMA is funding a series of programs, $13.4 million in FEMA money. And albeit some of the programs on the list may be important programs to be done, I am not certain they should be being done by FEMA. Of the $13.4 million they are going to have a year-long celebration of trees, gardens and other healing spaces called gardens and healing spaces, multicultural dialogue that includes a greater discussion of who we are, where we are from, why we are here and how we are doing. Theater workshops, building trust during war workshop, peace workshop and anger management workshop. And I don't know if that comes out of that program or elsewhere, and I am not necessarily

saying that some of these things are not good, but I think my constituents back home in Arizona think of FEMA dollars as going in after a disaster and doing more specific.

Chairman COX. Will the gentleman yield?

Mr. SHADEGG. Yes.

Chairman COX. If they are good, they certainly need to be renamed at a minimum. And if those are accurate descriptions I am skeptical that they are worthwhile.

Mr. SHADEGG. There may have been times that my wife would have liked me to have had an anger management class. I am not sure FEMA should have been paying for it, and I don't know how I feel about a peace workshop and I am not against peace.

In any event, Dr. Carnes, do you have a comment on either the evaluation done by OMB or on this program?

Mr. CARNES. As the guy who is on the receiving end of the grades that OMB hands out, it is a very effective club. I take them seriously because OMB then tortures us with the results and slashes our budget.

Mr. SHADEGG. I don't want to slash your budget. I want you budgeted to do what you need to do.

Mr. CARNES. It is incumbent upon us to do this right. And as much as any—half the time I would say the problem is we cannot say what it is we are doing. I said in response to an earlier question I want to know what the thing is that we are buying. Too often grant folks tend to talk about the process they are using. I am interested in the thing, then I can measure it. So sometimes it is just that the program cannot define what it is about very well or how it is going to do its job.

Sometimes it is because they just do a poor job of executing, then you have to either fix—you have to fix it. As to that project, it is an interesting project.

Mr. SHADEGG. Maybe I should give you this flyer and you could get back to us on those specific projects.

Mr. BERMAN. The IG would be interested in the flyer as well.

Chairman COX. Did that come from OMB?

Mr. SHADEGG. No, it came from a Northern Virginia community resilience project that was funded by a FEMA grant. I yield back the balance of my time.

[Information follows:]

FEMA DOLLARS AT WORK

$13.4 million taxdollars for:
Gardens and "Healing Spaces"
Multicultural Dialogue
Theatre Workshops
Building Trust During War Workshop
Peace Workshop
Anger Management

Post 9/11, FEMA granted funds to several counties in Northern Virginia to form the Community Resilience Project

According to its website, "The Project is made up of caring mental health professionals and outreach workers who are dedicated to help the community heal during these difficult times. The Project offers education, referrals, and counseling services, free of charge, to all individuals and groups within Alexandria City, Arlington County, Fairfax County, and Loudoun County." Source: http://www.communityresilience.com/

Some examples of Northern Virginia's Community Resilience Project activities paid for with FEMA dollars:

"*Common Ground* - The Community Resilience Project is collaborating with the Virginia Cooperative Extension and a group of other community organizations in a yearlong celebration of trees, gardens, and other healing spaces. An event held every month focuses on the theme of the healing power of our connection to trees and nature."
http://www.communityresilience.com/[illegible]

Multicultural Initiative

"The Community Resilience Project ... will present a series of cross-cultural dialogues. These cross-cultural dialogues are to encourage the community to participate in a greater discussion of who we are, where we are from, why we are here and how we are doing." [illegible]

Multicultural Town Meeting Thursday,
May 8th, 2003, Alexandria, Virginia

"Building Trust During War: Dealing with Differences and Embracing Commonality"
http://www.communityresilience.com/Information/Flyer-Tricia.doc

"3. Anger Management Program
This comprehensive program helps participants explore anger and its common causes, become familiar with anger cues, develop coping skills, manage feelings that accompany anger & develop a comprehensive anger management plan. Presented in 1 to 12 1.5-hour sessions. Ages teen to adult."
http://www.[illegible]

"Future Workshops to address issues of:

- Diversity
- Peace
- Violence vs. Non-Violence"

[illegible]

"Theatre Workshops - Our counselors also provide opportunities for children and teens to participate in several theatre activities. Plays from different countries are used to illustrate the similarities between community values despite differences in cultures." http://www.[illegible]

Chairman COX. Does any other member wish to be recognized for questions? I have one last question and that concerns again the grants.

Since 1999, Federal law has required that applications for these grants be made electronically and that the reporting also be accomplished electronically. Is that actually happening, Mr. Berman?

Mr. BERMAN. It is with regard to the ODP grants, basically the emergency preparedness grants. It is not happening with regard to the FEMA grants, the disaster assistance. Again—.

Chairman COX. That legal requirement does apply to FEMA, does it not?

Mr. BERMAN. I believe so, sir.

Chairman COX. Maybe, Ms. Springer, you could shed some light on why we are not in compliance.

Ms. SPRINGER. I may be able to help a little. As part of that grants modernization, that is law, P.L. 106–107, perhaps.

Chairman COX. The Federal Financial Assistance Management Improvement Act of 1999.

Ms. SPRINGER. That is right. As part of that the grants.gov is going on line with an E-find capability which in effect will be like a yellow book on-line for anyone to go on and find grants that may be applicable. First responder grants for localities. And secondly, there will be an E-apply capability that will be going live this fall, and under that capability an applicant who finds a grant will be able to apply on-line one time entering a set of information that could be utilized for any grants that may be plugged into that system in effect. So the applicant does not need to repeatedly enter the same information.

It is just a start. It is not in its full-fledged capability. But that is the Government-wide answer to making that applicable.

Chairman COX. What about the E-comply program since we have testimony that, quote, FEMA seldom used its enforcement power to compel grantees to fix problems even when the grantees had long histories of noncompliance? And FEMA was specifically cited in one category for serious fraud, waste and abuse.

Compliance is also, is it not, the subject of this same 1999 law?

Ms. SPRINGER. Yes, it is. And another thing that goes with that is the Single Audit Act, which requires audits of grantees. So that is another piece of this overall grants review to make sure that the money is going to the purpose for which it is intended.

Chairman COX. Dr. Carnes, do you want to comment on this? Because it is good to hear that we are aiming for legal compliance sometime in the indefinite future. But given that the noncompliance is so directly related to fraud, waste and abuse, this seems like something we want to leap on.

Mr. CARNES. It is a problem and we have got to fix it and fix it right away.

Chairman COX. I appreciate it. The committee will work with you on this and stay interested, because the creation of the Department is really an opportunity to fix these problems. These are problems that DHS inherited. DHS has been around only for month, not years, and so I look at this as an opportunity to fix the long-standing problems in the legacy agencies that you have acquired, to re-

configure them for the Homeland Security objectives and to do so with alacrity.

In that vein, Dr. Carnes, for what it is worth from the committee's standpoint, if the time for the issuance of the RFP that you described for the audit is either late winter or early spring, it would be very pleasing if it were late winter and not early spring. The faster the better. My concern is this: that very soon it will be the way we have always done it. So we have this opportunity now with the creation of this new department to change things that otherwise might be impossible in government to change. But if we let a year or two slip under our noses, then there is not only going to be the old INS way, there is going to be the DHS way and people that work at DHS will say this is the way we have always done it at DHS.

This is a golden opportunity. We will only get it once. Never again in the history of this cabinet department, which will probably live indefinitely, will this golden moment occur again. The faster the better.

Mr. CARNES. Yes, sir.

Chairman COX. Thank you for being outstanding witnesses. The hearing is adjourned.

[Whereupon, at 3:00 p.m., the committee was adjourned.]

APPENDIX

MATERIAL SUBMITTED FOR THE RECORD

DR. BRUCE CARNES RESPONSES TO QUESTIONS FROM THE HON. JIM TURNER

Question: **1. Would your office benefit from a capability within the Department involving the ability to carry out long-range strategic assessments concerning the nature of the terrorist threat facing the country?**

a. To your knowledge, does the Department possess, or plan to establish, such a specific capability, either in your office, the Under Secretariat for Information Analysis and Infrastructure Protection, or elsewhere?

Answer: The Under Secretary for Information Analysis and Infrastructure Protection (IAIP) will provide this capability. Actionable intelligence, including long-range strategic threat assessments, which can lead to stopping or apprehending terrorists, is essential to the primary mission of DHS. IAIP will fuse and analyze information from multiple sources pertaining to terrorist threats. This information includes foreign intelligence, law enforcement information, private sector data, and publicly available information. The Department will be a full partner and consumer of all intelligence generating agencies, such as the National Security Agency, the CIA and the FBI.

Timely and thorough analysis of projected terrorists threats and the projected threat environment is critical to the Department's ability to prioritize program and resource requirements to safeguard our homeland. IAIP will provide long-term vulnerability and threat assessments as input in preparing long-range planning guidance to support preparation of the Future Years Homeland Security Program (FYHSP). Program and resource requirements within the Department will be prioritized to counter projected terrorist threats.

Question: **2. Would an annual National Homeland Security Strategy document, which could include a comprehensive threat and vulnerability assessment, aid the Department's program and budget review process?**

a. In particular, would it assist you in developing internal budget guidance for the Department's components, which could result in an articulation of program and budget priorities over the five year span of the Future Years Homeland Security Program?

Answer: Yes, an annual National Strategy for Homeland Security would be valuable in helping develop program planning guidance, and for that reason the Department is developing an annual DHS Strategy. From that, the Department is building a long-term comprehensive planning programming and budgeting system to support the Future Years Homeland Security Program (FYHSP). The system will align resources to programs that support the Department's objectives, demonstrate accountability, are performance driven, have identified long term benefits, and meet the Department's priorities. As part of this system, the Department will issue an annual program planning guidance, based on the Under Secretary for Information Analysis and Infrastructure Protection's long-term threat and vulnerability assessment, the National Strategy for Homeland Security and the Department's strategic plan. The program planning guidance will:

- Provide guidance to the agencies in preparing their input to the FYHSP.
- Define the projected homeland security operating environment based upon threat assessments regarding the security of the homeland.
- Define the national homeland security priorities necessary to help achieve and maintain homeland security goals and objectives; and
- Ensure the necessary framework (including priorities) to manage Department resources effectively for successful mission accomplishment consistent with the National Strategy for Homeland Security.

Question: **3. What is the current status of the Department's initiative to consolidate the 83 separate financial systems, few of which are integrated, that it inherited from its legacy agencies earlier this year?**

a. What integration goals have been established, when will such goals be achieved, and how many financial systems is the Department planning to operate when consolidation effectors are complete?

Answer: The Resource Management Transformation Office (RMTO) working under the DHS Chief Financial Officer (CFO) has initiated the ***eMerge²*** Program to transform the business and financial management policies, processes, and systems of DHS into a single solution that addresses the financial management, acquisition, and asset management requirements for the Department. ***eMerge²*** is a business-focused program partnering the CFO, Chief Information Officer, Chief Procurement Officer, and Chief Administrative Officer to deliver a consolidated enterprise solution to DHS operators, policy-makers, and decision-makers.

Status

The RMTO has defined the strategic goals and developed the detailed program management plans and strategies (e.g., Risk Mitigation, Configuration Management) necessary to execute the program. The ***eMerge²*** acquisition strategy will integrate requirements development with alignment to the DHS enterprise architecture, while building in quality and program audit.

The ***eMerge²*** Program was reviewed and approved by the DHS Investment Review Board (IRB). (The IRB selects all major DHS programs that are to go forward, then controls and evaluates their progress. It is composed of top DHS Leadership, chaired by the Deputy Secretary of DHS and includes the Under Secretaries of Management, EPR, BTS, S&T and IAIP. The IRB provides approved programs with strategic guidance and ensures alignment with DHS missions, strategies and goals.) The approval of this program on September 24th designated ***eMerge²*** as a DHS program operating under the DHS CFO.

Plans

The program is divided into two major phases. Phase I addresses the core requirements that are common for all agencies in acquisition and procurement, budget formulation and execution, civilian pay and travel settlements, accounts payable, asset management, funds control, general ledger and reporting, and accounts receivable. The requirements definition will be complete by April 2004. Phase II, which will include delivery of a consolidated enterprise solution, will begin with implementation at one site in early FY 2005 and implementation at additional sites from March 2005 through FY 2006.

MR. RICHARD BERMAN RESPONSE TO QUESTION FROM THE HON. JIM TURNER

Question: **If the Department was formally made a part of the 1990 Chief Financial Officer's Act, would that make it easier for the Office of the Inspector General to monitor compliance with it, and, thus, assist in ensuring that federal resources are managed appropriately?**

Answer: As I mentioned in my testimony, even though DHS is not presently subject to the CFO Act, the current DHS CFO, to his credit, has pledged to comply with all of its requirements as if he were legally bound to do so. We applaud his position, and we will monitor and report on whether he adheres to it through our regular audits of department programs and operations.

While the current DHS CFO agrees to comply with the provisions of this law even though he is not obliged to do so, his successor may not take that position. If a future CFO were not to follow this law, we believe that it would be harder for OIG to obtain management's agreement to take any corrective actions we might recommend to address any deficiencies we might find in the area of financial management.