S. Hrg. 104–714

FEDERAL GOVERNMENT FINANCIAL MANAGEMENT

HEARING

BEFORE THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

DECEMBER 14, 1995

Printed for the use of the Committee on Governmental Affairs

U.S. GOVERNMENT PRINTING OFFICE

21–793 cc WASHINGTON : 1996

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402
ISBN 0-16-053949-8

S. Hrg. 104–714

FEDERAL GOVERNMENT FINANCIAL MANAGEMENT

HEARING

BEFORE THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

DECEMBER 14, 1995

Printed for the use of the Committee on Governmental Affairs

U.S. GOVERNMENT PRINTING OFFICE

21–793 cc WASHINGTON : 1996

For sale by the U.S. Government Printing Office
Superintendent of Documents, Congressional Sales Office, Washington, DC 20402
ISBN 0-16-053949-8

COMMITTEE ON GOVERNMENTAL AFFAIRS

TED STEVENS, Alaska, *Chairman*

WILLIAM V. ROTH, Jr., Delaware
WILLIAM S. COHEN, Maine
FRED THOMPSON, Tennessee
THAD COCHRAN, Mississippi
JOHN McCAIN, Arizona
BOB SMITH, New Hampshire
HANK BROWN, Colorado

JOHN GLENN, Ohio
SAM NUNN, Georgia
CARL LEVIN, Michigan
DAVID PRYOR, Arkansas
JOSEPH I. LIEBERMAN, Connecticut
DANIEL K. AKAKA, Hawaii
BYRON L. DORGAN, North Dakota

Albert L. McDermott, *Staff Director*
John E. Mercer, *Counsel*
Leonard Weiss, *Minority Staff Director*
Michal Sue Prosser, *Chief Clerk*

CONTENTS

FEDERAL GOVERNMENT FINANCIAL MANAGEMENT

THURSDAY, DECEMBER 14, 1995

U.S. SENATE,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Committee met, pursuant to notice, at 9:50 a.m., in room SD–342, Dirksen Senate Office Building, Hon. Ted Stevens, Chairman of the Committee, presiding.

Present: Senators Stevens, Brown and Glenn.

OPENING STATEMENT OF SENATOR STEVENS

Chairman STEVENS. I apologize for the delay this morning. Our hearing covers the status of Federal financial management issues.

My judgment is that the American public is frustrated with Government, resulting from a variety of factors. The public questions whether Government costs too much for the level of service it delivers. They want less financial waste and better program performance.

This Committee has addressed these concerns under previous chairmen, such as my friend Senator Glenn, who is here, and Senator Roth.

In past years, Congress passed three major bills to improve financial systems and program accountability—the Chief Financial Officer Act of 1990, the Government Performance and Results Act of 1993, and the Government Management Reform Act of 1994. These measures provide a solid statutory framework for improving Federal accountability and performance.

How far along are we on the path to satisfactory financial accountability? How much further do we have to go, and when can we expect to get there?

We are going to examine two new legislative proposals this morning. One is a package of amendments proposed by Senator Glenn to the Single Audit Act, and the other is an effort by Senator Brown to ensure that Federal accounting standards are implemented throughout the Government.

I might say that right after the first of the year, I shall ask the Committee to establish a new subcommittee to deal with the broad subject of general financial management because I believe that these acts and those we are proposing today should have very continuing oversight.

Senator Glenn?

OPENING STATEMENT BY SENATOR GLENN

Senator GLENN. Thank you, Mr. Chairman.

I think our Committee is a unique committee in that part of our written mandate is not only to oversee the organizational aspects of Government, but also the efficiencies of Government. That is a big order, and we are the only Committee that has across-the-board jurisdiction in these areas, across all the panoply of Government. And we have taken that seriously. Five years ago, the Chief Financial Officer Act of 1990 was signed into law—actually, it was 5 years to the day, on November 15th, when we had originally scheduled this hearing and had to cancel it—but I believe the CFO Act was one of the most important laws we have passed in the last 50 years. I know the Comptroller General testified at a hearing several years ago, when we had just put that in, I believe, that he felt it was the most important tool of financial management in Government in the last 40 years—5 years later now, I guess we can say 45 years instead of 40.

But prior to 1990, it is hard to believe that the biggest organization, the biggest financial operation in the whole world, the United States Government, had no requirement to do an audit of its agencies and departments every year. How did things go? We would just wait to see how much we spent last year, and we will put in a little more, and we will ask Senator Stevens on Appropriations to appropriate a little more next year and add a little bit because we know it's going to get cut back a little at OMB, and that is sort of the way we did our business. And that is a ridiculous way to run the biggest business in the world.

So prior to 1990, there was no requirement for a bottom line audit at the end of every year. So we are very interested today in seeing how this whole thing worked. We worked for about 2–1/2 years on the CFO Act with Dick Darman, who was over at OMB at that time, and with Mr. Bowsher here; we had many, many meetings, and staff meetings, and we finally put that thing together.

Just to point out some of the problems, GAO told us back then that the Federal Government had over 500 different accounting systems spread across the agencies, with hundreds in the Department of Defense alone. Later, they qualified that a little to make it that the Federal Government has at least 200 major different accounting systems. But they could identify 500 different accounting systems and 200 major different accounting systems. The Pentagon has 162 different systems, as I recall, and the Army alone has 43. So we are looking at a huge problem here, and we were literally in the Dark Ages of accounting. Some agencies were not even doing double-entry bookkeeping, something which was invented by an Italian monk over 500 years ago, as I understand it—I was not around at that time, but I understand he is the one who started double-entry bookkeeping.

Chairman STEVENS. Strom Thurmond audited it. [Laughter.]

Senator GLENN. Anyway, 5 years later, we have a very different picture because, strengthened by the 1994 GMRA, the Government Management Reform Act, the CFO Act requires annual audited financial statements of 23 major Federal departments and agencies. We are not clear across Government yet as far as our audit requirements are concerned, and that is one of the items I would like to bring up a little later and get your opinion on, Mr. Bowsher, as to how we go about spreading this more.

But I think we are driving real, honest-to-goodness reforms in Government. Systems are being upgraded. Agency CFOs are taking part in top agency management decisions. Government-wide accounting standards are being developed, and OMB and GAO oversight is spotlighting problem areas that need serious attention.

Now, everything is not fixed. DOD contractor overpayments and the IRS mess in accounts receivable are just two examples that show how far we still have to go. I trust our witnesses today will talk about those particular problems.

I hope we can also discuss legislation that may be needed. GAO, for example, has been working with my staff to draft revisions to the Single Audit Act that the Chairman just mentioned, and also, Senator Brown has a proposal to strengthen the accounting standards process. So I hope our hearing can build a record for any needed legislation, and that we can continue to move forward and improve Federal financial management.

We all talk about revenues and expenditures around here—it is a big deal, revenues and expenditures—but we too often leave out the middle part of that, which is how the money gets spent, and are we making the best use of every dollar. That is what we are talking about here, the efficiencies of Government, which should receive every bit as much attention as is given to revenues and expenditures.

One of our problems here is that this is not high-priority. When you talk about financial management, it is like MIGO—my eyes glaze over. You see what a huge crowd we have at each press table on both sides of the room here today and all the cameras that we have focusing on financial management here today. It is a MIGO item. But yet I think it is one of the most important items we have for the future of really restoring the confidence in Government that Senator Stevens mentioned a few minutes ago. How are we going to cut out waste, fat, fraud and abuse, which we roll off as just one term—waste, fat, fraud and abuse, it is automatic. Yet we do blessed little to try to cut out waste, fat, fraud and abuse.

We have taken a position on this in the past, and I commend Senator Stevens for holding the hearing. We look forward to hearing from Mr. Bowsher, Mr. DeSeve, and other witnesses this morning and look forward to your advice and your comments.

Thank you, Mr. Chairman.

Chairman STEVENS. We have three panels this morning. The first panel is the Hon. Charles Bowsher, the Comptroller General, and he is accompanied by Gene Dodaro, the Assistant Comptroller General, and Jeffrey Steinhoff, the Director of Planning and Reporting.

Mr. Bowsher?

TESTIMONY OF HON. CHARLES A. BOWSHER,[1] COMPTROLLER GENERAL, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY GENE DODARO, ASSISTANT COMPTROLLER GENERAL, ACCOUNTING AND INFORMATION MANAGEMENT DIVISION, AND JEFFREY STEINHOFF, DIRECTOR OF PLANNING AND REPORTING, ACCOUNTING AND INFORMATION MANAGEMENT DIVISION

Mr. BOWSHER. Thank you very much, Mr. Chairman, Senator Glenn. I know you have a very busy schedule these days, so I am going to try to summarize my statement.

First, I commend this Committee. As you pointed out, Mr. Chairman, this is the Committee that has passed the key legislation, beginning in 1990 with the CFO Act, followed by the Government Performance and Results Act in 1993, and then the Government Management Reform Act of 1994.

We now really have the legislative base to move forward and get the Federal Government into a modern accounting and auditing position, which is long overdue.

At the same time, I believe that we can report that real progress is being made. In other words, as we have done our financial audits in the last 3 or 4 years and through our work with the administration and the executive branch, we have seen, I think, more financial management improvement progress in the last 5 years than we have seen for several decades.

First, let me just say how pleased I am that OMB is playing such an important financial management leadership role in the executive branch. For many years, there did not seem to be that kind of financial management leadership from OMB, but there certainly is today.

Second, a cadre of qualified of CFOs is in place at agencies and, with few exceptions, they are actively seeking to make the needed improvements.

Third, the inspectors general are embracing their new financial audit responsibilities. Fourth, the much-needed new, comprehensive accounting standards, including cost accounting standards, are nearing completion, and efforts are underway to further strengthen the quality of federal financial reporting.

One of the big areas that the executive branch has yet to do is to put emphasis on modernizing financial systems. In other words, a lot of systems work is needed. But I am very pleased that the Congress put a financial statement audit requirement in law, because that will lead to improved systems.

One thing that we are concerned about is that we have enough resources to do the job as the inspectors general and we move forward with plans to do the audits, which are now required for all 24 of the major agencies starting with fiscal 1996. Also, starting with fiscal 1997, there will be annual consolidated reports to the American taxpayers, which GAO will audit.

At that point, if you think about it, we really begin to have the Federal Government on the same basis as Congress required the private sector after the stock market crash of 1929 with the Securities Act of 1933 and 1934. What the Congress really said was that

[1] The prepared statement of Mr. Bowsher appears on page 51.

if you sell securities to the public, you have to have an annual audit of your financial reports and some standard accounting principles on how you put those reports together.

Congress did the same for State and local governments after the New York City fiscal crisis in 1975. States or large cities did not routinely have comprehensive financial audits prior to that crisis, and then the Single Audit Act was passed in 1984, and that required it.

So what we are really trying to do is get the Federal Government, the last big part of our economy, to be able to properly account for its financial assets and its operations and to be able to provide reliable and relevant financial reports to the taxpayers.

And Mr. Chairman, I could not be more pleased to hear you announce that you are going to have a special subcommittee in this area, because I think it is really a very crucial area to regain the support of the American people for our Government. The Federal Government has got to be able to account for its funds as they come in, and all the assets that it has. As I said, the legislative base is there. Now the big thing is to carry it out. And I would hope that we could have the resources in the executive branch and at GAO to make sure that the government achieves the requirements of the various legislative mandates in the next couple of years.

One of the main things that must be achieved is more modern systems. We have testified before this Committee regarding the Defense Department, the IRS, and some of the other major agencies that have weak systems. They have acknowledged serious weaknesses in those systems and are working on them, and we hope they can make real progress in improving the systems in the next few years. I think that the personnel issue and the systems issue are really the most important that must be overcome.

The last thing I would like to cover is the Single Audit Act and the amendments now being considered. The Act is over 10 years old. Important experience has been gained in that decade, and very great progress has been made. The State auditors and the State governments today issue annual reports that can withstand the scrutiny of an annual audit. The amendments to the act being considered at this time would require summary reports, raise the threshold so some of the smaller governments would not have to be audited, and get the reports more timely.

So if the Committee can report out that legislation, I think it would certainly be a big plus.

I would like to close with that and would be happy to take any questions that the Committee would like to ask us.

Chairman STEVENS. Thank you, Mr. Bowsher.

We have not heard Senator Brown's statement yet. Do you have a statement, Senator Brown?

OPENING STATEMENT OF SENATOR BROWN

Senator BROWN. I do, Mr. Chairman, and I will try to make it very brief, with your indulgence.

I think what we are dealing with today is a terribly important point. It is natural that agencies would be concerned about their own flexibility—they would not be human if they did not. It is appropriate that the General Accounting Office be concerned about this, and it is appropriate that OMB be concerned about this. But the bottom line that I think concerns us is that we do not have generally-accepted accounting principles spread throughout the Federal Government. We literally keep our books in a different way, and it is the Tower of Babel when it comes to understanding our finances.

I do not know of a major enterprise anywhere in the world that does not have a standardized accounting system, either directly or indirectly. As I think everyone here knows, the one international language other than English—and English, as Senator Glenn knows from aviation, seems to be a pretty standardized language, at least in some areas—is our generally-accepted accounting principles that get modified somewhat in international areas but do provide an international language for communicating. So we are the only one that does not have that. It is terribly important if we are going to communicate effectively and administer effectively that we have it.

I think the tough problem that is before us as a Committee is figuring out how we can do this in a way so that the understandable concerns of any administration through OMB, the executive budget office, and their natural and understandable desire to control the way the books are kept for their administration, is somehow compatible with GAO, which in the past, we have charged with responsibility in this area, obviously, in the 1921 Act, in the 1950 Act, and in the modifications since then.

What I think is important, ultimately, is not that we crown someone, either GAO or OMB, to do this for us, but that we have some general standard. This bill has been dramatically rewritten to meet the objections of the administration, and really, their objections—there were a number of them, but the principal one was that there were sanctions in the bill if they did not comply. As you know, we have had general guidelines for accounting procedures in the past; the only problem is that people ignored them. So it is not that it is a new concept.

We have pretty well eliminated those sanctions in the hopes that we could bring the administration on board. But I personally believe this may be one of the most important concepts that we examine this year, and I want to thank you, Mr. Chairman, very much for having this hearing and for bringing it up and being willing to consider the concept.

Thank you.

Chairman STEVENS. Thank you.

Mr. Bowsher, when I was sitting down where Senator Brown is now sitting, I suggested a Department of Administration, and as I have moved up these chairs I have suggested a Department of Administration. Now I am sitting in this chair, and I want to ask you: What do you think about a Department of Administration?

Mr. BOWSHER. Well, I think it has some merit, Mr. Chairman. I do not know specifically what your plan would be.

Chairman STEVENS. My plan would be that we would consolidate the administrative functions of the Federal Government in one department, and all other departments would feed off of that. We would have one system of accounts, one system of reporting, we would have one system of collecting debts, and we would have one system of administration.

As you know, my State pioneered that when it came into the Union. It has one Department of Administration, and it works very well. We do not have separate accounts, we do not have problems with standardization. We have one system of accounts. What is wrong with that?

Mr. BOWSHER. In principle, there is nothing wrong with it, and it makes sense. I think for a State like Alaska, it probably makes a lot of sense. The one question I——

Chairman STEVENS. It works for the microcosm, but it will not work for the world; is that it?

Mr. BOWSHER. No. I am saying that what we could achieve here in the Federal Government is a lot of consolidation where you would get down to one, or where you would have, say, the Department of Defense as one, along with one or two others. I have often thought the Federal Government could get to about three accounting centers, you might say, but then consolidate financial information in one department. So if you had a Department of Administration, you would make it responsible for the central consolidation, like the corporate headquarters of a very large organization, and then bring in the information from two or three accounting centers.

Today, there is a finance center in New Orleans that has done a lot of consolidating, and GAO's accounting is now done down in New Orleans; it is run by the Department of Agriculture. If there are two or three of those kinds of centers working in the Federal Government, I would think that you could achieve what you are really driving for; that is, greater standardized, centralized administration. Whether you could get it all into one organization for a government as large and as diverse as our Federal Government, I have never been quite sure about that; but certainly a lot more could be done than is being done today.

Chairman STEVENS. Well, we do hope to have a reorganization plan up and pass it next year, and I think that is going to be my goal, to try to include in that a concept that the commission must consider that proposal. I hope that Congress will agree.

Now, you are looking at a number of reports that OMB is required to give to us, and the real problem is whether these consolidated reports are going to meet our needs here in Congress. I have some question about that in terms of where we are going, but do you see that those consolidated reports will have to be broken down again for us to deal with, let us say, appropriations or the various functions that we review?

Mr. BOWSHER. Well, you would probably have to have some backup information coming to the various committees, like the Appropriations Committee, but I do believe that pulling it together in one consolidated report does make some sense. We do it ourselves at GAO. I issue my annual report to the Congress, and it is no bigger than the average corporation report. We include in there a summary of our Financial Integrity Act control review, our annual financial statements audited by one of the big six accounting firms, a good description of our performance during the year compared to previous years, and so on.

So I think you can pull it together in a good summary form, and I think it would be very useful for the Congress to have annual oversight hearings of these major departments, just to see how they are doing in total.

At the same time, I think that some of the backup for some of the specific committees, like the authorizing committees and the appropriating committees, you would probably have to have some additional information flowing to you. But I think a consolidated report does make some sense.

Chairman STEVENS. Well, let me ask you about my two friends here. Senator Glenn has a package of amendments, including one on the Single Audit Act. And as I understand it—and Senator, you can correct me—that would require a single audit of a state's use of Federal money in a series of functions. Is that going to put a burden on states to look at it altogether at one time?

Mr. BOWSHER. No. The Single Audit Act of 1984 required a single audit and eliminated a lot of duplicate auditing. Prior to the passage of that Act, there was too much auditing of certain parts of the State governments—the Feds would come in with their auditors, the states would do it, the program people would do it, and so on. So this really streamlined the auditing of the States and local governments. But what is needed now are some amendments to that legislation, because for one thing, the thresholds which determine who has to have a single audit were fairly low when the law was enacted, and with inflation and so on now, they need to be raised. Also, some of the reports have come in on what I think is less than a timely basis. So the amendments would move the reporting requirements up by 4 months; and require a summary report, which would be more useful to the program people who are running these large programs.

So what we have here are some amendments that will make the Single Audit Act better. The States and the cities have proven that they can do this single audit. I think it is one of the real success stories that we have achieved in the last 10 years.

We have worked very closely with the State auditors and the State financial people in putting together these amendments, and OMB has, too. So I think we have a package here that is really quite good, and I would recommend that the Congress move forward with it.

Chairman STEVENS. Did OMB submit these, indicating that——

Senator GLENN. We had asked GAO to look at these issues and see what might be done to improve the Single Audit Act, basically, and then you worked with OMB and came back——

Mr. BOWSHER. That is correct.

Senator GLENN [continuing]. And then we met with you, and that is how——

Mr. BOWSHER. Yes. There has been a lot of coordination on these amendments.

Senator GLENN. The Single Audit Act—I think everybody is in agreement that that has been a good move. The states like it, and we will have testimony on that later today.

Mr. BOWSHER. Yes. I might point out, too, Mr. Chairman, that we have what is known as an "Intergovernmental Audit Forum" which was started by my predecessor, and that is where all the different auditing groups meet together. So I think in the last 20 years, we have brought together a much better auditing approach to the State and local governments, with the different levels of government, and that has been one of the successes.

Chairman STEVENS. Senator Brown has some amendments, and I understand OMB is going to take the position that the suggestions have merit, but that legislation is not needed.

You have taken a position in favor of these amendments?

Mr. BOWSHER. We have. I think the big issue is that we now have a good working memorandum of understanding between OMB, Treasury and GAO. The concept in the 1950 Act, which Senator Brown mentioned, was that the three units would work together and improve financial management. Over the years, it really did not happen, and I tried to get it to happen when I came into this office, but I did not get cooperation from OMB under Mr. Stockman. So it took us quite a while, but as Senator Glenn pointed out, under the Bush administration we finally got this memorandum of understanding worked out, and the three of us are working together. We have an independent board that is setting the new standards, and I think that within the next few months, we are going to be publishing the best set of standards that any government has in the whole world.

So it is working well. What the legislation would do is put a legislative base under what we have proven is working well here in the last 5 years.

Now, one of the logical questions is why do you need that legislation if it is working so well now, and I just think it is the old issue of putting some permanence into the system.

Chairman STEVENS. You currently operate similarly under a memorandum of agreement?

Mr. BOWSHER. Yes, that is right.

Chairman STEVENS. And this would confirm that so that it could not be changed without approval of Congress?

Mr. BOWSHER. That is correct.

Senator BROWN. Mr. Chairman, it is a little like asking that the parents of a child be married. We think a ceremony would be most helpful.

Chairman STEVENS. I want to confirm that mine worked despite some comments to the contrary. [Laughter.]

I wonder, do we have the reservoir of people in Government to do these additional financial tasks—and I am not saying it in any derogatory way—but we are piling on every year new financial requirements, and it may be soon that you accountants will outnumber lawyers in the Government.

Mr. BOWSHER. I do not think so.

Chairman STEVENS. Well, it sounds to me like there are more tasks for accountants now than for lawyers.

Mr. BOWSHER. Yes. Well, it is a very good question, Mr. Chairman. The two things that worry me the most in accomplishing everything we are trying to do are: Can we modernize the systems, and can we get enough qualified, technically trained, up-to-date personnel in the Government and keep them there? In other words, it is one thing to get them here, but it is sometimes a little trickier to keep people at these salaries in the Government.

Gene Dodaro has been working with Ed DeSeve over at OMB, meeting with the 24 agencies that have to have audited financial reports, and I think maybe Gene can give you a little more detail on where we stand on it, because I think the question you have raised is very pertinent.

Chairman STEVENS. Yes, sir.

Mr. DODARO. The real essence of this is not more people or even more money for financial systems, but it is making better use of the resources that are there. The people issue has consistently been found in financial audits—not following procedures that are prescribed in the agencies. The audits that have been done in DOD and the ones we have done in IRS have shown that the financial management personnel structure is badly out-of-date.

What we are dealing with is an organizational structure that has had years of neglect and a low priority. And as you pointed out, first-rate financial requirements have been placed on them now, and they have a big gap. They are beginning to close that gap by having qualified CFOs in place, and what they need to get now is the supporting structure. And what they really need to focus on—and this is something OMB and the CFO Council are trying to do—is to get the right mix and the right people in there.

So I do not think it is a question of adding numbers; it is a question of getting the right staff in there, with more up-to-date skills both in the systems area and in financial analysis capabilities.

This scenario, we are really concerned about; because of the current downsizing, it has to be done right. I think there are ample resources that exist there if they are used properly.

Chairman STEVENS. I do not know if you have read "Soldier of the Last War." There is a scene where the Italians, in running their army, had an enormous roomful of auditors who reviewed every request for deployment of troops, purchasing of equipment, and so on. And that is where the war was lost.

What I am asking you is when you are looking at all these things, are you following technology through? I mean, Wal-Mart used to have a whole series of financial offices all over the country, and they have one now.

It sounds to me like we are going the other way—we are having more and more financial managers built into every part of our system, and they are not connected together. That is why I would like to see a Department of Administration. So why is it that we have to have so many more additional financial management tools in each department? Why aren't we centralizing? Why aren't we saying just one—take the "management" out of Office of Management and Budget and make it work.

Mr. DODARO. The goal has been to try to get at least one unified system for each of the major departments and agencies, and agencies are trying to move in that direction. You are right, technology is important, and technology has not been used effectively in the financial management area 1), to simplify the process and reduce the number of people, and 2), to have uniform systems that can interact with one another.

Part of this problem is beginning to be addressed by the CFO structures. Previously, each component and each agency had its own ability to create information systems and accounting systems;

and now the CFOs need to bring that into a sort of unity and use technology.

You are exactly right, Senator. Technology is the key here in order to get more uniformity and reduce the number of people that you have. But we have seen, not only in financial management, but in other areas, where the Federal Government has not used technology effectively yet to streamline its operations.

Chairman STEVENS. Well, it would seem if you can agree on an interagency process, you could agree on an interagency procedure in terms of use of the same program and the same type of system and have all that information flow through to a central source without being crunched in each administrative office of each department, then crunched in the OMB, then crunched in GAO, and then crunched in every committee up here.

Mr. DODARO. You are exactly right. In fact, we often find there are still manual processes or manual manipulations that are required. And financial management organizations now in most agencies are armies of clerks at low levels that move paper around. What we are trying to do—and we are working with each of the agencies—is to eliminate that and go to single data entry and one source that can be drawn upon and used effectively.

So that is the intention, to move toward streamlining and simplification.

Chairman STEVENS. "Soldier of the Last War" should be mandatory reading for your people, Mr. Bowsher.

Mr. BOWSHER. All right.

Chairman STEVENS. I have got to stop here—but again, that is just what I am saying—we still have manual people out there. If one person decides that that person wants to change the world, all he has to do is change some of the numbers, and it will take you forever to find him.

Mr. BOWSHER. Mr. Chairman, if I could just add one thing which goes along with your thinking—take Australia. Some years ago, they did go to one accounting system and one budgeting system, and today, with PCs and so on, the Members of Parliament can look and see where things stand; the Treasury, which is kind of like the budget bureau, can look at it; the auditors can work off that one system; they can pay a bill here in Washington at their embassy and have it updated within 48 hours or something like that.

We could have that in the Government. We could have one system. My only concern is that the Federal Government is so large that you might have to have two or three processing centers. If you could get the Department of Defense down to one processing center, you would accomplish a great deal. And I was hoping that that was where they were heading, but then they started several centers.

Chairman STEVENS. My colleagues do not know it, but you know it—I suggested that you be the arbiter between OMB and CBO, and when I went into that meeting with the leaders, the answer was that that means there will be three computers rather than two. [Laughter.]

Senator Glenn?

Senator GLENN. We need a cost-benefit analysis of how many Government lawyers we ought to switch for accountants; maybe that would not be a bad idea.

Alice Rivlin has written to our Committee with a proposal to test streamlining management reports, as called for in the Government Management Reform Act of 1994. Do you think that should be approved? The obvious pitfall might be that in streamlining reports, we would cut out information that might be useful up here. Do you think we ought to try that?

Mr. BOWSHER. I think we should try it, and what they are calling for is a pilot, so I think it is well worth doing the pilot.

As I said, we have tried to get our report down to that one consolidated report, and I think if you look at the GSA report and the Social Security Administration report, they are very close to that, and it makes it much easier for the Congress and the senior administration people to read.

At the same time, your concern and Senator Stevens' concern must be recognized, that something does not drop through the cracks that is vital information. One thing I would be very concerned about is the controls. In other words, when you are reviewing the controls in the system, you have got to have a good summary of any weaknesses in that consolidated report.

I would think also, on the financial report, that you would not want the auditors certifying to a set of financial statements and then having just a few highlights listed in the consolidated report.

So there are a couple of concerns which I think the OMB people are taking our advice and other people's advice about, and I think doing this pilot makes a lot of sense.

Senator GLENN. In your statement, you mention the problem of accountability that follows any devolution of Federal responsibilities to the states. During the debates on the welfare and job training bills, for example, some IGs indicated that the block grant proposals might actually limit their investigation and audit authority, as well as reduce their resources.

What should we do to ensure that a proper audit trail will exist with block grants? And the background, to my way of thinking, is that it is not necessarily in a state's interest to find problems with how they administer a block grant if you are going to get some cut off. And I do not think most of us would look at State IGs as perhaps having the same reliability we would like to base future block grants on.

What can we do to ensure that a proper audit trail will exist with block grants and that there will be accountability there?

Mr. BOWSHER. I think basically, the states can probably do the financial audits and review the systems. The state auditors are really quite good; we have been working with them, as I mentioned earlier, over the years, through the Intergovernmental Audit Forums. So I have a lot of confidence in the State auditors.

At the same time, I think it is the program information that you have to be concerned about as to whether there is enough of an audit trail or requirements as criteria for the success of the block grant. So I would think that as the Congress passes that kind of legislation, it ought to think about requiring some basic information as to what would be viewed as the criteria or standards for the program's success. With such criteria, it would then be incumbent upon either the Federal program audit people or the state people to check to see if that is being carried out and whether that information is available. And then the third thing would be to actually evaluate the program to see how well it is being administered.

I think if you put those building blocks in there, you can achieve it.

Senator GLENN. Are we going to have to put those additional requirements in there, though, because right now the proposal is to send block grants back to the States? Is the system adequate so that we can keep up with auditing those funds right now, or are we going to have to have additional bureaucracy put in to monitor it?

Mr. BOWSHER. I would think that the resources to monitor and to audit it are probably there. I think the big thing will be whether the information is there.

Senator GLENN. Yes. In your testimony, you touched on the relationship between the CFOs and the IGs. There is a just-released survey by Coopers & Lybrand—and I think we will hear about that shortly—that perhaps there is some degree of tension between these two shops over their respective roles. For example, a high percentage of CFOs would just as soon contract out the financial statement audit function to a private sector accounting firm.

Is implementation of the Act affected by tensions between the CFOs and the IGs?

Mr. BOWSHER. I do not think so. I think we have seen a lot of progress. There was a lot more tension a few years ago, and I also think that the executive branch did not have the qualified CFOs that they have gained in the last year or two. And I think the IGs are starting to do a better job on their financial audit responsibilities.

I think the Congress wrote the CFO Act much as it did the Single Audit Act. In the Single Audit Act, it gave the responsibility to the States, and some States like Maryland, went out and hired CPA auditors to do the audit. In other States, like California, the State auditor did it, but he hired some of the CPA firms to do some of the major components, like the State university system. I think that that is what is happening here at the Federal level. In other words, it gives you flexibility. Many of the IGs now are hiring outside auditors to assist them.

So I think what we ought to do is go for 2 or 3 years here, see how the audits are done in 1996 and 1997. I think you are always going to have some tension between the CFO and the IG, but I do not think it will inhibit the Act being carried out, and I think we have actually seen progress made there in working together.

Senator GLENN. Your audit team has been doing an evaluation of OMB's recent reorganization, called "OMB 2000." I was interested to hear that prior to OMB 2000, OMB's Office of Federal Financial Management, OFFM, had 41 State positions, and now it has only 20—a reduction of 51 percent.

When they reorganized, they farmed these management people out, in effect, to be in OMB's budget offices. I was a little skeptical of that whole process, I must admit. What is your assessment of how that is working out? I know they farmed these positions out, but can OFFM do its statutory job—statutory job, now—with half the people it had before?

Mr. BOWSHER. Well, if they have the right people, I think they can do the statutory job. I have always been concerned about the level of staffing at OMB; even when they were at 40 positions, that is not a lot of positions to be trying to monitor the whole Federal Government, a $1.6 trillion operation.

I will say that I think the current team over there is the best team that I have seen at OMB in my nearly 30 years here in Washington, so I think they are doing an excellent job with the staffing they have. I think your concern, Senator, about whether they have enough staff, is a very valid one, and if you were to lose any of the key people at any time, or not replace them with staff of that capability, I think we could be in trouble. But right now, it is working very well. They have some fine people at OMB, and I think they are doing an excellent job.

Senator GLENN. Well, if these people they farmed out to the different places still operate as if they were still back in their original spot there, and report in, and do it with the same kind of analytical work that they were doing before, then I think the whole thing will work. But I was afraid that once they got out and got into all of these different branches that there would be a tendency for them to be sort of preempted by where they were as much as by what their job was supposed to be. Do you have any opinion on that at all?

Mr. BOWSHER. No, I do not have an opinion on that, and it might be good for you to ask Mr. DeSeve about that.

Senator GLENN. Yes. DOD keeps coming up as our financial management problem all the time. The CFO Act requires agencies to report on their financial operations. Despite this fact, the Department of Defense still cannot perform that basic task. I am sure this is one reason why GAO has designated defense financial management as "a Government-wide management high-risk area."

In fact, I understand that in our "high-risk lists," as we call them, in which you make an annual assessment on and which OMB does, too, that DOD is still in the very highest risk as far as financial management is concerned. Is that correct?

Mr. BOWSHER. It is correct, yes. It is one of the agencies that we worry the most about in the next couple of years. As I have testified before, we are very pleased that Secretary Perry and the Controller, John Hamre, have readily admitted the problems and that they have a plan to do something about them. But going back to an earlier question, do they have enough qualified personnel to really achieve it—that is one of the big questions, and so I do worry about the Defense Department.

Chairman STEVENS. If I could interject——

Senator GLENN. Yes.

Chairman STEVENS [continuing]. But that is just my point. Why are we hiring more people? Why don't we go to the other point of consolidating functions so we need less people?

Mr. BOWSHER. Well, I would agree with consolidating those functions at the Department of Defense, but you have got to redesign the system when you do the consolidation, and you need technically qualified people to do it. I am not saying hire more people. What

I am really saying is that you need staff today that understand modern computers and modern communications systems, and I am not sure John Hamre has that many there to be able to achieve it.

So that as you consolidate, you have to have talent to know how to do that consolidation. I think they have gotten into some trouble with the DFAS system because they tried some consolidation and lost control.

Mr. STEINHOFF. Let me add a thought to that, Chairman Stevens.

Chairman STEVENS. Yes.

Mr. STEINHOFF. About 40 percent of the Federal accounting systems are over 10 years old, and in DOD, their systems are in real bad shape. They have an estimated 80,000 accountants and financial managers. That is a lot of people. But they are working with a blizzard of paper and very old systems. If you get the systems into better shape and, as you said, consolidate the operations——

Senator GLENN. Is that the major problem?

Mr. STEINHOFF. They have bad systems, and they have a clerk-driven type of financial process.

Senator GLENN. Well, I have been out to the DFAS center, and I could not agree with you more. You have different DFAS centers—some have retirement accounts and so on that are just the epitome of excellence; they really are. I was almost shocked. A call comes in, it is answered, all the stuff comes up on the screen, the guys are there, and they have an answer for people just within a minute or so, on a lot of this stuff.

Then you go down to the other center, where we are paying out all the big money accounts, and these people are running little carts down through a warehouse to pick up manila folders off of metal racks. I took some out and laid them out just to look at them, and that is how people are paying our bills. And as a result of that system, a couple of years ago, we had contractors who returned over $700 million. They sent it back, saying, hey, we never sent you a bill for this.

Mr. BOWSHER. That is right.

Senator GLENN. And so we looked into some of those accounts, and we found another $750 million or so, so that was over $1.4 billion. And part of the problem may be the Prompt Payment Act, perhaps, which says you must pay within 30 days, so if somebody thinks a bill is coming up, they are going to pay it because they do not want interest to be charged on their watch as a result of the Prompt Payment Act. So we have a real morass here, either a problem with a law or with outdated practices, and it seems to me we ought to be able to straighten it out.

Computerizing accounts should help. I understand they are making progress in it, but it is slow, and it is like pulling teeth.

Mr. BOWSHER. Yes.

Chairman STEVENS. Yes, but you modernize by computerizing from the very first input, not from how to handle those manila envelopes faster. That is the problem, and we cannot seem to get anyone to understand that if you have a system and teach everybody the new system, it is a heck of a lot better than molding the old systems and folding them in until we finally get a new one.

Senator GLENN. That is right.

Mr. BOWSHER. I agree with that, yes.

Chairman STEVENS. Well, Mr. Bowsher, I respectfully think it is your responsibility to see that it comes about.

Mr. BOWSHER. Yes. Well, we certainly are trying to work with the Department of Defense. I think if you could ever get out to Columbus, Ohio—which Senator Glenn suggested I do, and I did do it, and John Hamre had a lot of industry people there that same day——

Chairman STEVENS. My family migrated from there in 1890, and I have not seen any reason to go back. [Laughter.]

Mr. BOWSHER. Well——

Senator GLENN. There must be an answer to that, but I cannot think of it at the moment. [Laughter.]

Chairman STEVENS. What was your point—sorry.

Mr. BOWSHER. Well, my point is that what you would see in Ohio is the current system, and you will see how it has to be modernized, as you are saying, with modernized computers and so on. You will also see that when they moved it and consolidated it, or tried to consolidate the old systems, they lost control. That is what you do not want to happen.

So I think a trip to Columbus gives you as good a snapshot of what the problems of financial management are in the Department of Defense as any place you could go.

Senator GLENN. They are making a lot of progress; I do not want to imply that things are all bleak. But it is slow, and I do not know how you put new accounts in under a new computerized system, and let the old ones sort of fizzle out as things go on; that is a major problem. They are just trying to keep their heads above water out there with the resources they have, and they are doing a pretty good job with the resources they have.

Do you think we need more resources? Do they have money enough to devise and operate a good system?

Mr. BOWSHER. Yes, I think they have enough money. I think they spend billions on new systems, and they are not successful, so that as Gene mentioned earlier, I think it is not a matter of getting more people or more dollars; I think it is a case of having the right people who really know how to do it, how to bring the modern systems into the Government.

Senator GLENN. And your summarized statement this morning indicates the magnitude of this thing. You say on page 5 of your short statement, "For example, as of August 1995, DOD reported $28 billion of problem disbursements, of which $16 billion had remained unresolved for over 180 days. Also, each year, hundreds of millions of dollars of overpayments are voluntarily returned by DOD contractors."

This is not a small problem. We fuss like crazy over a billion here and a billion there around here, and here, we have $28 billion.

Let us go to IRS. How are they coming? That is one of our favorite topics here. For instance—this is quoting out of your statement—"We found that IRS had $65 billion in delinquent taxes, not the $110 billion shown on its financial statements, and of the $65 billion, we estimated only $19 billion to be collectible." Now, that is down, because a couple of years ago, it was up to $32 billion.

But $19 billion out there that is collectable, and we do not have either the system or the people or the agents—that is collectible. These are not the bankruptcies, individual or corporate. These are collectibles, they estimate, that we just do not go out and get. How we would love to have $19 billion spare money around here right now, with the balanced budget problems we have.

Every year, we used to have a hearing on TSM here. We would have the IRS in, and every year—well, we think it is going to take 5 or 6 years to fix the problems. Then we would go on to the next year, and they would testify again—5 or 6 years to fix the problems. And we would go on to the next year, and we would hear 5 or 6 years to fix the problem. It was a rolling target, and we did not seem to be making any progress.

Are they making progress now, and what is your opinion on IRS?

Mr. BOWSHER. They are making progress, but they have not made enough that we can give them a clean opinion on the audit.

On the TSM, I will have Gene give you a few words on that, because that is where we do have some concerns that they are not making as much progress as their plan intended, and I think the Congress has taken some action to try to improve it.

Mr. DODARO. On the tax system modernization effort, we issued a report last July that was very critical of IRS' technical and managerial capability to carry that out. We made about 20 or so recommendations to really build their capabilities in this area until they have a good strategic plan in place.

We found, for example, that their ability to develop the software themselves for the new systems was at the lowest level possible and that they did not really have the processes in place to be able to do that. Their processes were kind of ad hoc, chaotic, and not repeatable.

So we made a number of recommendations. We are waiting for them to respond to our recommendations now, and we are going to continue to evaluate what kind of progress they are making.

We were pleased that they accepted the recommendations and promised to implement them. The Commissioner made a commitment to do that; whether or not they actually follow through and put the recommendations in place I think really remains to be seen.

Senator GLENN. Do they have the resources, once again, to do it?

Mr. DODARO. The resources are there. It is just a question of getting the right people. For example, their tax system modernization executive left. They have replaced that person. They are looking for a chief information officer. And it is really an issue of bringing in the right people; it is not a question of additional people.

Also, IRS needs a CFO. Their last chief financial officer left, and they have not yet replaced that person. We have urged IRS for years to go outside the Federal Government to bring in a qualified chief financial officer and a chief information officer who have installed large-scale systems in the private sector of the type that the chairman was talking about and you have talked about, Senator Glenn, because part of the problem is that in installing these new systems, you have to go outside the financial management boundaries. This occurs in Defense, for example. The contract payment process starts with the contracting process at DOD in the first place, and that whole process needs to be streamlined and modified, and you need people who can understand that and have done that successfully.

So it is just a question of the right people. It is not more people, and it is not more money. It is people who have done this successfully.

Chairman STEVENS. I have gone way over my time.

Senator Brown?

Senator BROWN. Thank you, Mr. Chairman.

I wanted to take you back a little bit to get some of your observations. If I understand our current system correctly, we basically have a system where accounting and reporting standards are laid out by the GAO, budgetary standards are laid out by OMB, and monthly and annual cash-type reporting duties fall under the province of the Treasury. And our 300-some departments and agencies each of the ability to set up their own accounting systems. Over this, we have laid the FASAB board, which will provide some guidelines.

But in reality, no one person is responsible when there is a breakdown in any of these areas. At least that is my impression. I wonder if you all would comment on that or correct me if I have misstated it.

Mr. BOWSHER. That has basically been the system in the Government. What the CFO Act, which you have already passed, and the new standards would say is: here is one set of accounting standards that everybody has to apply. Through this legislation, you are now really going to be holding 24 chief financial officers responsible, which represent 95 percent of government expenditures, so you have got the bulk of the government in those 24 agencies. Then, if you could do some consolidation with the systems—as I said earlier, you do not need 24 separate systems out there; I think you could do some consolidation. It seems to me that you would then know who is responsible for the financial reporting. Also, you are going to get financial audits at the end, just like you do in the private sector and in the State and local governments.

So in the next few years here, you are going to be transferring from the situation which you just described very accurately—that is literally the way the government has limped along since World War II—to something that has accountability and hopefully has some modern processing systems.

Senator BROWN. Mr. Chairman, my impression is that any bright person—and our Government is filled with bright people, and we have been blessed with very intelligent people—the first thing they think about is not putting together a report that emphasizes their deficiencies. They tend to think in other terms. And what we are doing is leaving in people's hands the ability to report on themselves, and it should not surprise us that it does not always work, and it should not surprise us that it is not always unbiased.

So at least I think the step forward is to get clear uniform standards and some pinpointing of responsibility, and at least my view is that this is our best path out of the quagmire that we have gotten into in terms of accounting standards.

Mr. BOWSHER. I think we have a good plan here, and now the question is whether the Government can achieve it.

Chairman STEVENS. Well, I would add to that some requirement that somebody—and I would hope it would be you—is constantly inventorying the development of technology to see how the system can be improved. That is what Wal-Mart had that we do not have, and I think someone has to—I was going to ask you if you have a section of technology implementation, and bring it in so it is applicable to Government procedures. Someone out to be there, reaching into this new digital information and saying, "This will work better," and trying to see how we can do it.

It is true that we cannot buy every generation of new technology, but we can start adapting every generation of new technology, and we are not doing that. I would hope that we know where we are going.

I was at the other meeting this morning, on telecommunications. Computers will soon be talking to computers by radio and not by electronic—by direct connections with cable—and I think we are going to find a whole new system with the digital system, which we will not be using, but the rest of the Nation's economy will be using. I think he is right that we must get standardization, and we must get someone at the point to say we are about ready to change gears, and this is where we are going.

Mr. BOWSHER. That is right.

Chairman STEVENS. But everybody is changing independently, and that is why his law is necessary, in my opinion, because it holds us to some standards and says to everybody, You keep it this way until you change it, Mr. Bowsher—until you change this system, it is going to stay the same.

Mr. BOWSHER. You are absolutely right. I have a small group, not nearly as large as I would like, in the technology and systems area. We have issued some guidelines and reports on how to go about it, and we have been working quite a bit with Senator Cohen. The fact is that Government has not gotten the payoff from its investment in systems because it has ended up with too many different systems, which is the point that you are concerned about.

We worked with the Army on the medical supplies, to show them how it is being done in the private sector. At first, the Army was skeptical; but they have now instituted private sector practices. They did it by hiring a retired Navy captain who went to work for Wal-Mart and found out how Wal-Mart systems work. He has now literally put it in the Army. Walter Reed does not have any more inventory tied up in, say—the one we compared it to was Vanderbilt's medical center—whereas a few years ago, they had four times as much money tied up there.

So you are absolutely right, these systems have to be modernized. Technology is moving very fast, so you have to, as Gene pointed out, bring in the expertise of the private sector and utilize it.

Chairman STEVENS. Sorry, Senator Brown. Please go ahead.

Senator BROWN. I am finished.

Chairman STEVENS. I will only make one comment and then go to Senator Glenn. At one time, I found up in Pennsylvania a warehouse full of the bars that you put over the tops of sedans to make them into police cars. You just put this thing in, plug it into the cigar lighter, and you've got the flashing lights up there. You can press a little button, and you can get all red going, or you can get the green going. There was a warehouse full of them, and someone had run across a great deal of them and bought literally a 10-year supply for the Government, but failed to tell the Department of Defense that they were there.

Now, in my judgment, that could not happen to Wal-Mart. They are not going to have some place in Alaska that has a 10-year supply of anything, because the system is totally centralized.

Now, we have got to get there, and I do not see how we are going to get there unless your people take the lead.

Senator you have some questions.

Senator GLENN. Yes, the bar light thing is another one. We followed through on that one, too; we had testimony here once about bar lights in a warehouse that will last us out to the year 2012 or something like that. Every year, they were getting in another so many hundred, but they did not have space for them in the warehouse, so they had to put them under a tarp out back. They did not have a place to put them, and they just kept getting more, just because nobody had plugged all this into the system.

Is the Prompt Payment Act part of our problem?

Mr. BOWSHER. I do not think so. The problem basically is the antiquated systems in Columbus. The Prompt Payment Act basically says you should pay the vendors within 30 days, and if you cannot, you should pay them some interest. I think that is very fair.

Senator GLENN. Yes, but the employees are there, pushing the checks out, so that they are not criticized for an account getting behind that they have to pay interest on.

Mr. BOWSHER. Yes.

Senator GLENN. So they are erring on the side of sending the money out instead of bringing it back in. I have forgotten the amount of money that goes out of there, but it is something like——

Mr. DODARO. It is about $1 billion a day.

Senator GLENN. Yes. It is $35 million per hour.

Mr. BOWSHER. Yes.

Senator GLENN. It comes out to something like that.

Mr. BOWSHER. But you see, they should have good systems that can do that within 30 days.

Senator GLENN. This puts you on the spot, and maybe you cannot answer this, but you had a long personal employment in a major accounting firm for this country.

Mr. BOWSHER. Right.

Senator GLENN. As a result of that, you became Comptroller of the Navy, and now, here you are. You have been in the position for—what—11 years, 12?

Mr. BOWSHER. Fourteen and a half.

Senator GLENN. Fourteen and a half, all right. When you are having fun——

Mr. BOWSHER. When you are having fun, time goes by quickly.

Senator GLENN. Right. Now, I could not find anybody who could possibly have more experience in this area, but maybe this question is unfair. Using your level of expertise in advising us in the Congress, which you do, and that is your purpose, how long do you think it should take DOD to get their accounts in order so they can be auditable, and IRS as well? Those have been the two most vexing things, the two that we first looked into that you were charged with analyzing, and they have been an absolute unmitigated mess.

Mr. BOWSHER. Yes.

Senator GLENN. One is the biggest account in the world that anybody spends, that is, DOD; and the other account, IRS, is the contact point for every American once a year. And when they find out that IRS has their accounts all screwed up, and yet they expect the individual to be Simon pure in every, single bit of his or her own accounting, it does not sit well.

How long do you think, in your level of expertise, it should take if they went to work on this? Should it be by the year 2000, by 1998—for DOD and IRS?

Mr. BOWSHER. I think if you really had the right talent working on it, that you could get most organizations into good shape in 3 years. We got New York City in shape in 18 months—I always remember that—so that they could be audited. If you can get New York City in shape in 18 months, I think you can do the same for a lot of organizations—because New York City could not even reconcile its cash.

Senator GLENN. Well, you qualified that, though. You said if they have the right personnel.

Mr. BOWSHER. Yes, you have to have the right personnel.

Senator GLENN. Well, do they have the right personnel?

Mr. BOWSHER. No. As we have said here——

Senator GLENN. Well, then, under existing conditions——

Mr. BOWSHER. You are not going to get there in some of the areas. Now, I think you will at IRS. I would hope that IRS could get a clean audit opinion next year—if not next year, certainly the following year. I think they have made that much progress. But they will not have their total TSM system in.

But I think many of these Government systems, where they plan for 5, 10, 15 years, makes no sense at all. I think what you really ought to be doing is looking at 3 years, 5 years on the outside, of real change and real modernization. That is what they do in the private sector.

Senator GLENN. Well, I know that progress is being made—I do not want to be so gloomy—but we have been at this for many years. I have probably done a dozen hearings just on DOD financial management, and we go on year after year after year after year. And there is progress being made—we went to DBOF which has its own set of problems, and I think that is working out—I hope it is. But progress has been agonizingly slow, and I am glad to hear your estimate of 3 years. Maybe we can use that as a standard when they come over and testify and see what the plan is and how much progress they are making. Maybe we can set milestones to accomplish it within 3 years.

Mr. BOWSHER. I think Congress should start to set that kind of tight deadline for progress, because that is the only thing that is really going to accomplish it. You have to guard against accepting long timeframes. I remember going to meetings in the early seventies on IRS modernization. They always had a 10-year plan, which just does not make any sense. And generally, when you have a 10-year plan, you have a current, short-term thing that is not getting there.

Senator GLENN. And the target dates have always been rolling targets, too; that is the problem.

Mr. BOWSHER. Right. That is a very good point.

Senator GLENN. You know, you start to mentally make a note that by nineteen-something-or-other, you are going to have that thing fixed, and the next year it has slipped a year, and it just continues to be a rolling target out there.

Mr. BOWSHER. Yes.

Senator GLENN. We will submit any other questions. We have gone on a long time, and I appreciate it.

Senator BROWN. Mr. Chairman.

Chairman STEVENS. Yes, sir.

Senator BROWN. I would like to make just a brief observation if I could with regard to Senator Glenn's line of questioning, because I think he hit the nail on the head, and perhaps Mr. Bowsher would agree or disagree—I do not know.

But my limited experience indicates that the problem here is not just one of the accountants getting things in proper shape. At least in business, the biggest problem that we had was that it was difficult to get management to take the time to sit down and lay out what kinds of reports they need to do a good job of managing. Until you really get management engaged, the process does not get complete. So at least my sense is that it involves more than just the accountants getting their act together; it involves management thinking it through.

I will give you an example that I think is helpful. I remember a few years ago, talking to someone from the Nixon administration about how President Nixon had ordered people to spend all the money they could just before his reelection to beef up the economy. At least that was the way he described it, and I personally believe that was the intent of the orders that went out. And my understanding is that the Defense Department went out during that period and bought up a 3-year supply of toilet paper. The comment was: You have no idea how much a 3-year supply of toilet paper for the Army is. And they had filled almost every warehouse in the country—but it did goose up the economy for the election.

The point is not the creativity of the Nixon administration in getting reelected—obviously, they seemed to accomplish that—the point is that we did not have an accounting system that showed we had a 3-year inventory of toilet paper. The people who were doing the books and doing the reports were also the ones—well, the people who were giving guidance to the Defense Department to buy a 3-year supply of toilet paper also had control of the accounting system, which never reported to the public you had a 3-year supply of toilet paper.

Maybe we will never have another Richard Nixon as President—and I will not say that is good or bad—maybe we will never have anyone who gets carried away again—but I think the danger we have in the system also leaves it open to management abuse and gives management the ability, through its control of the standards, to not only abuse the system at times, but then to hide the abuse.

At least my sense is that that is part of the problem that we have right now.

Mr. BOWSHER. Yes, and I think it is important to get management involved in this. In other words, it is not just the accountants. What you must do is get the Cabinet officers and the heads of the agencies directly involved. That is why I have always thought it would be very useful if Congress held an annual oversight hearing of these 24 largest agencies starting with the audits for fiscal year 1996; ask them where they really stand, what progress they are making. Have not only the CFO and accountants there, but just as you would in the private sector, you would have the chairman of the board and the Cabinet officer at the same hearing.

Senator BROWN. Thank you.

Thank you, Mr. Chairman.

Chairman STEVENS. Thank you very much, Mr. Comptroller General. We have taken a long time, and I hope the other witnesses understand the reason. You are sort of our focal point in this whole endeavor, and we want everyone to realize that. We look forward to working with you. Thank you very much.

Mr. BOWSHER. We do, too, Mr. Chairman. Thank you.

Chairman STEVENS. Our next witness is Ed DeSeve, Controller of OMB. Ed, do you have someone with you?

Mr. DESEVE. No, sir; I am alone.

Chairman STEVENS. Gentlemen, let us put a little constraint on ourselves now, and limit ourselves to 10 minutes. We have another panel to hear from this morning, and I do want to be courteous and get to their testimony also this morning.

Mr. Controller, we are pleased to have your testimony. You may proceed as you wish, and we will put your full statement in the record, as we did with the Comptroller General.

TESTIMONY OF G. EDWARD DESEVE,[1] CONTROLLER, OFFICE OF FEDERAL FINANCIAL MANAGEMENT, OFFICE OF MANAGEMENT AND BUDGET

Mr. DESEVE. Thank you very much, Mr. Chairman, and I will try to summarize my statement quickly.

I am pleased to be here today to provide an overview of the state of financial management in the Federal Government. In my written testimony, I have drawn heavily from the July 1995 report entitled, "The Federal Financial Management Status Report and 5–Year Plan." This report, required by the Chief Financial Officers Act, reflects an overview of the status of Federal management and plans for improvement. The report was jointly prepared by the Chief Financial Officers Council and the Office of Management and Budget. I have extra copies if the Committee would like them.

I want to thank the Committee again for the work that it has done and the work that GAO has done in supervising the CFO Act, in restoring the public's confidence and trust in Government. The CFO Act is one of only several pieces of legislation that this Committee has sponsored, all of which build a sound foundation for better management of Federal resources.

The CFO Act and its subsequent modification by the GMRA and the GPRA of 1993, as well as earlier legislation such as the Federal

[1] The prepared statement of Mr. DeSeve appears on page 67.

Managers Financial Integrity Act and the Inspector Generals Act together establish a framework for improved accountability and better information for decisionmaking by Congress and the President.

I would also like to call special attention to the work of the Chief Financial Officers Council. The CFO Council is composed of all the CFOs and the deputy CFOS, and now, 24 agencies subject to the CFO Act.

Since May of 1994, this Council has taken a leadership role in setting Government-wide priorities for financial management. The three top priorities set by the Council this year are improving financial systems, implementing the Government Performance and Results Act, and issuing accounting standards and financial statements.

The Chairman has asked that I address the status of the CFO Act, GMRA/GPRA implementation, and the role of Congress in assisting in the implementation of these statutes, as well as OMB's plan for the consolidating of certain financial reports into an accountability report, proposals regarding the Single Audit Act, and Senator Brown's proposed Accounting Standardization Act. My written testimony covers these matters and other priorities of OMB and the Chief Financial Officers Council.

As important as these issues are separately, it is even more important to view them as an integrated whole. This perspective was expressed by Senator Roth, when he was Chairman of this Committee, and Senator Glenn, in a December 8, 1994 letter to Comptroller General Bowsher, in which they stated that a practical management framework is needed to coordinate the management reforms that have been enacted.

At OMB and in the CFO Council, we are seeking to create this integrated framework that will allow the administration and Congress to connect resources to results in the context of agency strategic plans.

As Mr. Bowsher has already testified, I would like to pause a moment and, as he did, thank GAO very much. This working relationship that we have with GAO and with our friends in the Treasury has been extremely important in carrying out this Act. As Mr. Bowsher indicated, we are making good progress. There are well-qualified individuals holding CFO and deputy CFO positions in all 24 agencies. Agencies are working toward the goal of integrated financial information systems of the kind the Chairman spoke of earlier. This is the CFO Council's number one priority.

Over the past 2 years, the number of separate agency financial management systems has actually decreased by 7 percent. OMB in the past 3 months has met with all 24 CFO Act agencies to discuss their progress and plans for improving financial management systems. These meetings provided information about the status of agency systems as well as a look to the future.

Mr. Chairman, I will digress for just a moment and say that the CFO Council has taken very seriously your comments today about technology and are in the midst of working with their counterparts in private industry and with some of their counterparts in State and local government. They will have a report in the spring of the year, which I will make sure the Committee gets a copy of, to look at the next 3 to 5 years of technology and see how Federal agencies can move forward to implement that technology. I think it is going to be a very important report, and we want to send that up to you as quickly as we can.

In terms of audited financial statements, another critical requirement of the CFO Act is that agencies prepare and audit statements for pilot organizations and all commercial, trust, and revolving funds. We have seen a marked improvement in agencies' acceptance of the rigors of financial statement preparation since the passage of the CFO Act. By mid 1995, almost 60 percent of the 100 entities preparing audited financial statements had received unqualified opinions.

In terms of the Government Management Reform Act, this Act expanded the requirement from audited financial statements to all of the activities, not just the trust and revolving funds, but all of the activities of the 24 CFO Act agencies, thus making the statements organization-wide.

GMRA also required that a Government-wide financial statement be prepared and audited for fiscal year 1997. OMB, GAO and Treasury are working with agencies to assure that both of these requirements are met.

In terms of accounting standards, underlying both the CFO Act and GMRA is the need for a comprehensive set of Federal accounting standards and principles. To have an audited financial statement without accounting standards is like playing tennis without a net—you really cannot do it.

Before 1990, the Government did not have a set of accounting standards. The Federal Accounting Standards Advisory Board, FASAB, was established on October 10, 1990 by the principals of the three agencies. It includes both representatives from Federal agencies as well as outside experts in accounting standards. I believe the board has been highly effective in taking into account a broad range of views and providing extensive comment periods to assure that implementation will begin as soon as the standards are issued.

What we have seen in fact in FASAB is very rapid progress, especially compared to FASB and GASB, the Government Accounting Standards Board that supervises state and local standards, as well as the Financial Accounting Standards Board, which supervises private sector standards.

Turning around in a very few years a set of, as the Comptroller General said, very good standards I think is something that they should be applauded for. By early spring, FASAB will have recommended a comprehensive framework for Federal reporting and the basic standards necessary to carry it out.

Once issued by OMB, these standards become generally-accepted accounting principles for executive branch agencies.

The Government Performance and Results Act is intended to bring about a fundamental transformation in the way Government programs and operations are managed and administered. GPRA requires that the Federal Government prepare strategic plans and annual performance plans, and submit annual reports which compare actual performance with goals. GPRA's implementation, legislatively mandated to take full effect in 1997, is well underway. In its statutory role as coordinator, OMB has issued two important documents on the preparation and submission of strategic plans in September of 1995. The first was a memorandum from Director Rivlin entitled, "Strategic Plans, Budget Formulation and Execution." The second was a revision to Circular A–11 on the preparation of annual budget submissions.

When I talk about integration, one of the most important aspects of integration is to integrate budgetary information and performance information in a unified way. To have performance information by itself, without knowing what it costs, is virtually unusable to Congress. In order to know what it costs, we have to have accounting standards, we have to have accounting systems which can accurately report the information. Knowing the purpose of the agency, we need to have strategic plans. To do that, the Chief Financial Officers Council has recommended—and we would like to spend a good deal of time talking with this Committee and then move on and talk to the appropriators—two annual reports in cycle, the first being a planning report that includes the strategic plan of the agency—that is, its objectives as well as its resources plan—that that plan be annually made available to Congress, essentially at the same time the President's budget is presented to the Congress; and an accountability report which wraps together all of the information currently in audited financial statements, in Federal management financial integrity reports, CFO Act reports, GMRA reports, CFO reports, and so on.

And if I may digress for a moment—and I realize this is a bit of a prop—I asked the Veterans Administration if they would give me the reports that they currently use for those purposes. I did not ask them to screen them in any particular way; I just said, if you would send them over, I will bring them up when I go up to see the folks on the Hill.

These are the fundamental reports, both the budgetary reports and the accountability reports, that come forward each year from the Veterans Administration now. And I did not say, "Give me the biggest stack you have"; I said simply, "Send over what you have."

They have begun the process, as have others, of prototyping what an accountability report might look like, a report that would allow the public, that would allow the press, that would allow the Congress to look at how are we doing, for example, in the speed with which we pay veterans' claims.

I have another report that just came in—and this report replaces about half of this stack; it does not replace all of it, but it replaces about half of this stack—I have another one that just came in from Social Security, and Senator Brown earlier made a very good point about people not liking to report on themselves.

I think you will find, as you go through this—and I will be happy to make this available to the Committee—this is for fiscal year 95, the fiscal year that just ended in September, so we think it is very timely information. But Social Security reports in the first real page of the report that only 48 percent of the people in this Nation have confidence in the Social Security system. Their first goal is to try to restore confidence in the system. They then spend a significant amount of time talking about how long it takes them to pay a disability claim.

When my mother went to get her own disability insurance benefits some years ago, I was appalled at the amount of time it took in that process. Honestly, Social Security says it has not gotten that much better. They have a standard to measure it against.

So I think this report, which combines the audited financial statement with a clean opinion—they have a clean opinion on their financial statement, and have had for some years—with performance information, both efficiency information as well as broader impact information—they talk very clearly about when the actuaries think that SSI is likely to come out of money, and there is a graph in here that demonstrates that. It is not a proximate problem, but if you can see the graph, it is a fairly dramatic representation of what happens some time in the future.

Senator GLENN. Could I ask a question here?

Chairman STEVENS. Sure.

Senator GLENN. It is fine to have a summary like this. The Chairman here is also one of the very senior members on the Appropriations Committee. When he is over there, trying to put an appropriations bill together and supervise all the Subcommittees, they cannot operate on a summarized view of things. They have to have specific, line item, dollar figures, dollars and cents, to put in the appropriations. They cannot do it just on generalized figures. If this summarizes those other things in enough detail, and they can do that, then this is a big step forward. If not—if this is a summary that is not useful to him—then it does not seem to me like it does much.

Mr. DESEVE. You are absolutely correct.

Senator GLENN. What is the status?

Mr. DESEVE. This, as I indicated, replaces about half of the reports. This is, if you will, the audited financial statement and the summary of performance of results. What we need to do is spend time with this Committee, with OMB, and then with the appropriators to find out how to create a similar document on the front end of the appropriations process.

One of the things that I am particularly uncomfortable with is the idea that the administration requires departments to submit to the President budget information. They then have to resubmit different information to the Congress. Well, if it is good enough for the Congress, it ought to be good enough for the President. We would love to find a way to have a seamless transmission, working with the appropriators, of detailed performance information and financial information that meets their needs, and we need to spend some time working with them to find out how to do that. This is only the back end.

Chairman STEVENS. Well, respectfully, that is not enough, in my opinion. I think we ought to have what the Comptroller General said Australia has. We ought not have to have your come up. We ought to have the ability to look at the reports you have and analyze them before you come up, and we ought to be dealing with the same numbers.

Mr. DESEVE. I agree with you, Senator.

Chairman STEVENS. We ought to have the same printout available to us, or the same computerization that is available to you, and we ought not to have this constant bickering about what the numbers are. We need just one set of numbers.

Mr. DESEVE. Mr. Chairman, I agree with you completely.

Chairman STEVENS. Why don't you put out a contract and ask for a proposal for some of these major concerns of the country, to design a system for the Federal Government, period, for the whole Federal Government, and put it into effect?

Mr. DESEVE. Mr. Chairman, we would like to do that. The design of the system, as you know, is a four-step process—analysis, requirements determination, design and implementation.

Chairman STEVENS. Well, just put out the contract. I can write that contract and get you a bid very quickly. It might take a year, but why don't we do that?

Mr. DESEVE. The first step in writing such a contract—to write a contract, we would like to get the appropriators to show us the kind of information they would like to have, so that as we design the——

Chairman STEVENS. No, no. I want you to get the kind of information you need to run the Government, and then we will use the same information to see how much more money you need every year. I do not need to have one designed for me. I need one designed for you. And I do not know why we do not put it out and get it.

Wal-Mart, again—and I do not have any stock in Wal-Mart; I wish I had—but I have got to tell you that they just went to an accounting firm and said, "Design us a system, and put it into place," and they passed up every company in the country.

Why can't we do that?

Mr. DESEVE. Like Mr. Bowsher, I would love to see that happen——

Chairman STEVENS. I will get you the money next year.

Mr. DESEVE. OK.

Senator GLENN. He will do it, too.

Mr. DESEVE. Yes, sir, I believe that.

Senator BROWN. Mr. Chairman, could I be argumentative for a moment?

Chairman STEVENS. Senator.

Senator BROWN. You have put your finger on exactly the problem, and I do not know if you have a response, but the problem you have is that I really think he is right—to do a good job for you, he needs—and I am being personal, but I think it comes down to every Cabinet Secretary and every chairman of an appropriations committee—he really needs guidance as to what it is you want, what concerns you, what you want to have highlighted, and he can put together a system that will do that. But what happens so often, at least in the private sector, and I suspect—although maybe I am wrong—I suspect here, is that you probably get very few Cabinet Secretaries who sit down with him and say, "Here is what I want your reports to highlight, and here is what would be a good guide for me to see if we are functioning properly." And I will bet there are very few Appropriations Committee chairmen who sit down with him and say, "Here is what I want to see," whether or not the agency or department is functioning.

I interrupt with that because I do not think any of this works without the management, the appropriations Subcommittee chairmen, or the Secretary getting personally involved.

Mr. DESEVE. It is our fault, too. It is our fault for not having asked. It is our fault for not having spent more time trying to develop the single system that the Chairman refers to.

I would like to comment for just a moment on the Wal-Mart model. When you look at corporate America, there are really two different models. The Wal-Mart model is a single, integrated firm which does essentially the same kinds of things within the firm. The other model for firms is what I will call the General Electric model, the holding company model, where the large steam turbine generator division, where General Electric Credit Corporation, where—they own one of the TV stations, and I have forgotten which one—NBC—actually are very different kinds of enterprises and require very different kinds of information coming up to a consolidated reporting framework at the management level.

What we have decided to do within the Federal Government is begin the process by designing for each of those enterprises, each of those entities, as GE does, an accounting system that meets management's needs. That is the process that is undergoing now that Mr. Bowsher referred to in the 24 CFO Act agencies.

Our challenge is the next step—this was my point about looking forward to the next 3 years—it is to integrate all of that information at the top so that it is useful across Government and then have the ability to use that system without destroying the operability of each of the agency or entity systems that are being created. That is the strategy we have chosen rather than a one-size-fits-all, to allow 24 entities to design one that fits for them, and then to find the commonalities because there are commonalities in those and, hopefully, as the Defense Department is doing, migrate, for example, to a single pay system. DOD has a very effective strategy. They have looked across the military systems and they have said, "We are going to take the best system and migrate to that system." And we believe that that is an appropriate step, but it is a process that has three or four steps to it. Unfortunately, we think moving to a single system would blur some of the utility for particular agencies.

Chairman STEVENS. I would like to move on to our next panel in about 5 minutes, but let me just make one statement and ask you a question.

The difference between GE and Wal-Mart is that Wal-Mart is a horizontally integrated company——

Mr. DESEVE. Correct.

Chairman STEVENS [continuing]. And you are looking at GE, which is a series of companies that are vertically integrated to a management system up here, and you have to decide which vision you have for the Federal Government.

My vision is the Wal-Mart vision because I do not think we ought to have a system in here so that one series of Government becomes more important than another, and that is what happens as you go up the vertical system. And you can make a choice, but my question is why did you pick the GE model?

21-793 O - 96 - 3

Mr. DESEVE. I think the GE model was picked because of the great differences among the agencies and their roles and missions. Again, even setting aside the Defense Department, which is very large, the mission of the Department of Housing and Urban Development is very different from the mission of the Environmental Protection Agency. One serves the public directly by providing housing and other services through State and local governments; the other is a regulatory entity that regulates and monitors and establishes liabilities over time. So they are very different. And then, when you throw the State Department into the mix, which is a direct service agency, there really are—and I do not mean to belabor this—different accounting issues.

One of EPA's big problem is how do we value Superfund sites and the liability for those sites. HUD's big problem is how do we monitor income eligibility, and a system that does not monitor income eligibility does not help HUD; one that does does not help EPA.

So that is really the reason why we started with that strategy.

Chairman STEVENS. Well, I will show my prejudice by telling you that my eyes are an appropriator's eyes, and I see all of those entities out there doing two things—either spending taxpayers' money or bringing in taxpayers' money—and I think there is a horizontal thing.

Senator Glenn, go ahead.

Senator GLENN. Thank you.

What are your comments on the pilot program that Alice Rivlin has asked for, the streamlining initiative?

Mr. DESEVE. We feel very strongly that, again, on the accountability side—not in terms of what an appropriator might need—that we would like to show the Congress in this pilot program the benefit of moving toward that consolidation so that it is easier for the public to get information, so the press can go through these reports on a timely basis, and that the Congress can, in one place, have one-stop shopping.

Senator GLENN. OK. I think that is a laudatory goal. I am concerned that we not streamline to the point where we do not get all the information we need; obviously, that is my concern.

Mr. DESEVE. Yes, certainly.

Senator GLENN. On the Single Audit Act, does OMB agree that the amendments—I assume you have had a chance to look at those amendments—do you agree those are needed?

Mr. DESEVE. We have not looked at all of the amendments. We understand the principles that are behind them. We do agree that they are needed. We think that raising the threshold—right now, if you get $25,000 from the Federal Government, you get audited. We think that $300,000 is enough, and we think you ought to evaluate that every couple of years to see if it should be moved up.

Senator GLENN. And we give you some flexibility in doing that—you would have some judgment that you could raise it above the $300,000.

Mr. DESEVE. Yes, we do, and what we would do is we would interpret that to allow State and local governments to substitute things that they thought were better for the single audit.

Senator GLENN. OK. In OMB 2000, your reorganization resulted in a shrinking of the statutory office you had, OFFM, from a staff of 41 down to 20. I know they are supposedly working in other places and so on, but do they report back to you, or how do you do that? I guess the basic question is are you still able to do your job with only 20 people?

Mr. DESEVE. Well, we do not like to talk about this because what we have done is we have created a Trojan horse——

Senator GLENN. Well, I think this is a good place to talk about it, right here.

Mr. DESEVE [continuing]. We have created a Trojan horse here, in each of the resource management operations. One of the criticisms of the management side of OMB is that it never talked to the budget side. So we sent our agents out into the budget side; we have them burrowed into the budget side, and whether it is cash management, or whether it is debt collection, or whether it is getting the budget people for the first time to look at an audited financial statement, understand and interpret it—GAO just did a draft report that Mr. Bowsher——

Senator GLENN. Question: Aren't these people being paid by where they are and not out of your budget?

Mr. DESEVE. By where they are; yes, sir.

Senator GLENN. OK. And their loyalty is still to you?

Mr. DESEVE. Well, sir, we do not like to ask them that question.

Senator GLENN. Yes. Well, when they first proposed this thing and first briefed us on it, that was my question. I did not see how you are going to put people out without having them preempted out there, wherever they are. You have to have absolute trust that these people are feeding you back all the information you need or the system does not work right, it seems to me. Is it working? That is the question?

Mr. DESEVE. I think it is. Yesterday, we had a need, very quickly, within a couple of hours, to prepare some answers to some legislative questions. I called on the people who had formerly been in our organization, for example, and asked them questions about IRS. They used to be in our place. I asked, "How are they doing?" Within 10 minutes, I got a response back from that individual, giving me chapter and verse of what was going on there. And we had other situations that were very similar to that yesterday.

Senator GLENN. Since these people are supposedly reporting to you, but they are being paid out there, have you had any cases so far where their boss, the guy who is paying them, has said, "Hey, I'd just as soon you did not tell old DeSeve this stuff up there, because this will hurt things a little bit here; I do not think he should know this." Have there been any cases like that that you know about?

Mr. DESEVE. None that I know of. In fact, it has actually been the reverse. We believe our folks have infected the budget side of the house with the need for better financial management, giving us a lot of leverage. Instead of losing 20, we think we have probably gained 200.

Senator GLENN. Do you think you can continue to do the OFFM job with just 20 people the way you are organized now?

Mr. DESEVE. Yes, sir, and they are very good people; we thank the Comptroller for his comments.

Senator GLENN. All right. More responsibilities are going down to the states the way Congress is moving and the way things are going right now. I am concerned about accountability. Do you think that the IGs can follow this money down the pipeline? Do they have authority to go down and monitor these things, since they are Federal dollars, that are going back to the states for the states' use? The definition of how the money is to be used is pretty vague in some of these programs, as I understand it, even to the point in some of them where, if the state does not use the money for its intended purpose, it can go back into the state treasury. That is pretty loose. Can the IGs still track this money down and get accountability? How does that stand?

Mr. DESEVE. We have concern as you do about how this monitoring is going to occur. We currently have a thing called the Medicaid Fraud Unit, which is audit that works with State governments, and there has been a very good relationship between HHS's IG and the State governments, because we jointly share—because we jointly fund, we jointly share that responsibility—although Medicaid is not proposed for a block grant by the administration, I use that as an example. If we were to have no responsibility, we would be very concerned about the states' ability to track fraudulent cases and use those funds properly.

So we share your concern. It varies program by program. And again, I only used Medicaid as an example. But we share your concern, whether it is AFDC, or JTPA, that that needs to be very clear, that the Federal IG must have oversight and must have responsibility for those Federal funds as they go to State governments, especially in the area of fraud.

Senator GLENN. We have had Federal funds going to State governments for a long time, but not to the magnitude that is being proposed here, as I understand some of the proposals. And if you see cases where legislation is needed to enable the IGs or somebody to follow these funds down and make sure there is accountability, why, let us know as soon as possible because this Committee would be the one that would probably have to take action on that.

Mr. DESEVE. What I would like to do if I may is to put this on the next agenda of the President's Council on Integrity and Efficiency, which is the IGs, and ask them to put together a very quick response for you that we will send up as soon as they have it done. In this case, it may take us 30 or 45 days from the time of the next meeting, but I would like to really spotlight that for you if I can.

Senator GLENN. Good. We would appreciate that.

Do you think Mr. Bowsher's estimate that DOD and IRS can have auditable accounts within 3 years is realistic?

Mr. DESEVE. Yes, sir. I think our friends in DOD will have accounts that can be audited, that are auditable, in compliance with GMRA for 1996, for fiscal year 1996. I think we will see the first comprehensive DOD audit in 1997. It will not have a clean opinion. I think it will take another 2 to 3 years from now to have a clean opinion in DOD, and there are many issues that have to be dealt with.

Senator GLENN. Is that a priority?

Mr. DESEVE. Yes, sir, I think it is. And again, when we talk about DOD, we have to give great credit to some of the services. I think the Army and the Air Force have done an exceptional job of anticipating GMRA and complying with it. I think some of the retirement funds have done an exceptional job. Our friends in the Navy, we do not know yet; we need to find out where they are.

Senator GLENN. Yes, there has been a lot of progress made. We are all doom and gloom over here sometimes, but I think there has been a lot of progress made. But I am interested in when we can get the whole problem really under control, and he thought it could be done within 3 years.

Mr. DESEVE. I would defer to him.

Senator GLENN. I want to talk to him about that and see what they think and set a goal, because I am now interested in setting some milestones and saying that you accomplish this by a certain time or else.

Mr. DESEVE. He is the auditor. Mr. Stevens, if I may embroider on one of your comments earlier, the Duke of Wellington before the battle of Waterloo is reported to have written a letter back to the Chancellor of the Exchequer, giving him a choice. He said, "Sir, I may either fill out the forms of your auditors and accountants, or fight a war, but not do both." Wellington obviously chose Waterloo, a particular course of action.

Senator GLENN. That is all. We can submit any additional questions for the record.

Chairman STEVENS. Senator Brown?

Senator BROWN. Two quick questions. You mentioned the effort to develop recognition of the commonalities in developing this system, and you also mentioned that you hope to have some progress this spring as you put things forward. Where are we with regard to the concept of standardized accounts, that is, an "account" meaning the same thing in the Department of Energy as it means in the Department of Commerce, and having some basic accounts which are fairly descriptive across-the-board?

Mr. DESEVE. I think the implementation of the standard general ledger has been—and I always use as a "cheat sheet" my report here—the implementation of the standard general ledger has been our benchmark so far for that, and we are at about—and I am doing this from memory—at about 60 percent across agencies in systems which implement the standard general ledger. And that is the first step, as you indicate, to having a code of 503.5 meaning the same here as it does there. All of the agencies are moving in that direction, and every new system that is being built implements the standard general ledger. It is a question of migration and how quickly we migrate toward that.

But that standard is very clear, and agencies are moving toward that standard general ledger very quickly.

Senator BROWN. Just so that I understand it, you have sent out to those agencies a list of accounts that they should work toward and a description of what those standardized accounts should cover?

Mr. DESEVE. Actually, we did it slightly differently, and this is something that is very important to being able to get our work done. We convened a group—and I am going to say about 3 years ago; I was not involved in the beginnings of it—from all of the agencies across Government, including Treasury, OMB and GAO. And every month, they meet and agree—because every once in a while, you will get a change in definition—they agreed, they put in place what they believed the standard general ledger categories were, so that when implementation came around, every agency had a representative who had been on the Committee and could help them install and interpret what that SGL was. So it is really more the work of a group rather than OMB slapping on the table, "You will do it this way."

Senator BROWN. What I was concerned about is, as we go through this process of trying to find areas to control expenditures, where I would run into it was the fact that in a number of expenditure areas, we did not have a standard account that would reveal, for example, how much a department had spent on travel, or how much had been spent on printing, or how much had been spent on rent, and so on.

Is there a way that your office could forward to us a breakout of what might be thought of as the overhead accounts and their descriptions?

Mr. DESEVE. We will do our best to try to get that to you, yes, sir.

Senator BROWN. I would appreciate that very much. It is one of the intriguing things because, at least in business, the kinds of things you might look at first, I found—and you might correct me, if you would, on the record—but I found the kinds of things I would have looked at first in business to cut, we did not even have a way of ascertaining how much was spent on them. If you think that is a fair or an unfair comment——

Mr. DESEVE. I think it is a very fair concern. It is easier on a department-by-department basis, but it is harder across departments.

Senator BROWN. Yes. Well, I think that is why your work is so vital, and I look forward to anything you might send me.

One thing I might just mention, Mr. Chairman, is that it strikes me the Congress has put you all in somewhat of an awkward position, which is not the first or the last time it will happen, with regard to, at least thus far, the decision not to pass a debt increase. As I understand, one of the things that the Secretary of the Treasury is trying to do to keep things afloat is to coordinate the management of funds out of the trust funds. And I do not want to use the wrong term, because I think he is in a tough spot, but I guess my question is: Is there an accounting standard that FASAB or you have put forth that deals with trust funds and the debt limit?

Mr. DESEVE. I do not believe the debt limit has been specifically addressed. It would come in two or three different standards. Let me look at that and get back to you on it. I do not believe the debt limit itself has been explicitly addressed. It is a very good question.

Senator BROWN. Well, I raise it because it strikes me that with a statute that puts a limit on how much we can borrow and then interpreting that, obviously, it becomes critical to the Secretary of the Treasury as he tries to keep funds available for operation. And the interpretation of that, it strikes me, comes down to in this circumstance how you classify the use of trust fund money. And that, I would assume, would be an accounting standard or would be dealt with through an accounting standard. Am I on track there?

Mr. DESEVE. I do not know, and I would like to give you a glib answer. I do not believe that we have a parallel, either in—in the private sector, we do not have a parallel. In State governments, the standard of compliance with laws and regulations which you are familiar with, which we do have in FASAB, suggests that you look to the law, that you look to the regulation and interpret the debt limit which is in statute, appropriately, interpret the trust fund mandates appropriately.

I do not know that the standard—I know that in government accounting for state and local, it does not go beyond that; it does not specify that you shall have a debt limit of X or Y, because it recognizes the limit that exists in each state. So I suspect that the standard in this case will point to the law and—it is a bit circulate, I admit—will say you must——

Senator BROWN. It would not necessarily involve an accounting standard?

Mr. DESEVE. I do not believe that it would, but I would like to research that and check with our friends at FASAB. I honestly have not been faced with that question before.

Senator BROWN. It is an intriguing question.

Mr. DESEVE. It is a very intriguing question, and I am glad that you do not have the answer to it, because I do not have the answer to it, either, without doing some research.

Senator BROWN. Thank you.

Chairman STEVENS. Thank you very much. I am sorry to cut you off, Mr. DeSeve, but I do want to get on to these gentlemen who have been waiting, also. We appreciate your courtesy, and we get your point from those reports, all right.

Mr. DESEVE. Mr. Chairman, thank you very much.

Chairman STEVENS. Thank you.

Chairman STEVENS. Our next panel includes William R. Phillips, a principal of Coopers & Lybrand; Kurt Sjoberg, California State Auditor; and Ted Sheridan, Chairman of the Committee on Government Liaison for the Financial Executives Institute.

Gentlemen, what we will do now if it meets your approval is to ask each of you to testify, and then we will ask questions to the extent that there is time remaining. I do not want to really limit you, but I would hope that you could keep your statements to somewhere around 10 minutes, so that we can all get out of here sometime after 12.

But you have been very patient, and it is a very serious subject for us, and we appreciate your willingness to come and share your views with us.

Mr. Phillips?

TESTIMONY OF WILLIAM R. PHILLIPS,[1] PRINCIPAL, COOPERS & LYBRAND

Mr. PHILLIPS. Mr. Chairman, Senator Glenn, Senator Brown, thank you for the opportunity to represent Coopers & Lybrand here today. I am William Phillips, a principal in the firms' Government

[1] The prepared statement of Mr. Phillips appears on page 74.

consulting practice located here in Northern Virginia. We are a group of 600 management, finance, and information technology consultants, focusing much of our effort on helping Federal agencies deal with the issues around the Chief Financial Officers Act, GPRA, and GMRA.

In my testimony today, I would like to share with you some of the results of a survey of Federal agencies, addressing the issue of implementation of the CFO Act. The results have shown strong support for and progress in implementing the Act. The Committee and Congress should be proud of having helped to make this legislation a force for fiscal and program progress.

However, the survey also reveals some issues that Congress needs to address in order to ensure continued support and progress.

This past summer, Coopers & Lybrand and the Association of Government Accountants surveyed nearly 100 Federal agencies to assess the status of their implementation of the CFO Act and related legislation. We surveyed 124 senior financial managers, CFOs, and deputy CFOs, 26 of the inspectors general, and 150 program managers—the customers, in many respects—collectively representing about 70 percent of the agencies covered by the Act. I would like to summarize the key findings in three areas—leadership, benefits and progress—a number of things we have already talked about here this morning.

As relates to leadership, there does appear to be broad support across the Federal Government for implementing the CFO Act. Seventy-five percent of the senior financial managers, 81 percent of the inspectors general, and 66 percent of the program managers—and that is what was, I think, striking—noted broad leadership support for implementing the Act. We defined "leadership" in the survey as the Secretary, the Deputy Secretary and the assistant secretaries. Very few of them felt that leadership was a problem.

As to the benefits, several of them are clear, and again, some of them have already been highlighted here this morning. All three groups agreed that the benefits of the annual financial statements justified the initial costs and efforts toward that end.

The inspectors general overwhelmingly agreed that the CFO Act has contributed to improved financial operations. Specifically, 88 percent of them reported improved financial systems, 96 noted some improvement in financial data, and most significantly, 100 percent of them recognized that as a result of the Act and related legislation that internal control procedures were improving. Both the financial managers and the inspectors general agreed that the process of developing the statements is more valuable than the actual statements themselves. The process contributes to a better understanding of what Government costs are and what drives those costs.

To gauge each agency's progress along the path of implementation, we reviewed the responses of the most senior financial managers—again, the CFOs and deputy CFOs—of the 71 agencies that participated in our survey and from the 26 offices of the inspector general. Nearly 80 percent of the financial managers reported that they are now preparing most of the documents and reports required by the CFO Act and GPRA. Although much work does remain in the area of performance measures, 86 percent reported at least partial progress. Progress was reported also in terms of integrating financial statement information into the budget process by about half of the respondents. Unfortunately, the flip side of that is about one-third said they had not begun to do that.

The bottom line is that 70 percent of the financial managers and 62 percent of the IGs believe that their organizations will have auditable financial statements by the March 1, 1997 deadline.

Chairman STEVENS. Say that again, please.

Mr. PHILLIPS. Seventy percent of the CFO organizations and 62 percent of the IGs believe that they will have auditable fiscal year 96 financial statements.

Chairman STEVENS. Where will the balance work in 1997?

Mr. PHILLIPS. Excuse me?

Chairman STEVENS. Where do you think the balance are going to work in 1997?

Mr. PHILLIPS. I am—I——

Chairman STEVENS. Well, you are telling me, if I hear correctly, that 76 percent are going to comply with the law.

Mr. PHILLIPS. I think the balance are not sure that we are prepared to do that, frankly. The key thing is auditable financial statements. I think you will have agencies that will prepare financial statements, but whether a statement is auditable or not is a very different thing.

Chairman STEVENS. It is my understanding that they must have it for fiscal 1996—that is the law. I find that a very interesting statement. Pardon me.

Mr. PHILLIPS. And again, what we have done here is we have asked them—we have not dug into what each of their respective positions is, but just asked them what they thought would be the situation.

Along those lines, there are some other significant challenges that they both face. Both groups felt—again, the CFOs and the inspectors general—that the lack of integrated systems is the biggest challenge they face. Second, insufficient funding was viewed as a barrier that needs to be overcome. Additionally, the inspectors general felt that the lack of supporting documentation, which gets to the issue of auditable financial statements, is their greatest barrier to accomplishing an effective audit of CFO Financial Act statements.

These findings are consistent with the issue of lack of integrated systems as being the greatest barrier. If the systems are not integrated with the management systems, it is going to be difficult to develop financial statements, and the auditors will be unable to render an opinion due to lack of consistent data or, potentially, a situation of incomplete data.

The financial managers and the IGs were clear that downsizing and budget cuts are affecting their operations. Only one-third of the financial managers reported that their offices received additional funding to implement CFO Act requirements. However, nearly two-thirds of the financial managers and a majority of the inspectors general noted that downsizing and the National Performance Review's emphasis on streamlining administration are in fact hampering their implementation of the Act.

In conclusion, the survey shows that there has been substantial progress by most agencies over the past 5 years. Moreover, there appears to be a wide acceptance of the CFO Act within the financial and audit communities, as well as with the program managers.

In closing, I would like to offer two recommendations to facilitate continued implementation of the CFO Act.

The first 5 years of the Act were characterized by Congress requesting financial and program information from agencies, sending them scrambling to collect, analyze and report the data. That was hard for them to do in many cases, but much good has come from that effort, as witnessed by the survey respondents. But that is not enough to sustain the effort.

This year and in years that follow, it is important that Congress use the financial statements when deliberating that organization's budget requests. This would visibly integrate the intent of the Act into the budget process and address one of the questions that we have heard a lot from them when their concern is that if the financial statements do not help us somehow, some way, in terms of budget requests, it becomes difficult to put the full force and intent of the efforts that you need to meet that Act in place.

Second, implementing the requirements of the CFO Act and related legislation requires organizational change and resource support. It is therefore important that Congress protect the offices of the CFO and the offices of inspector general from excessive downsizing cuts, while still holding them accountable for improved financial management and reporting, customer service and cost-effective operations. These improvements are both necessary and important. Investing a few million now to implement the CFO Act can yield billions of dollars of savings in the future.

Supporting the Act is smart business, and we applaud this committee's efforts toward that end.

Mr. Chairman, thank you for the opportunity to appear before you today. I would be happy to provide you with copies of the survey; I believe your staff have copies of it. And I would be happy to answer any questions you might have.

Chairman STEVENS. Thank you. We will have some questions later.

Mr. Sjoberg?

TESTIMONY OF KURT R. SJOBERG,[1] CALIFORNIA STATE AUDITOR

Mr. SJOBERG. Good morning. My name is Kurt Sjoberg, and I am the State Auditor of California. It is a pleasure to be here this morning to talk with you about Federal financial management, and perhaps more specifically as it relates to the Single Audit Act.

I am going to wear two hats this morning. One is that I am chair of a committee of our National State Auditors Association that oversees the single audit, but I am also the single auditor, performing the independent audit of California, which is the largest single audit in the nation. So we do have several points of view that are from our own, and my colleagues, the other state auditors, as well as that from the specific of California being the largest State.

[1] The prepared statement of Mr. Sjoberg appears on page 77.

Chairman STEVENS. Do you work for the state or for the legislature?

Mr. SJOBERG. I am independent of the legislature and the Governor both. We are under an independent commission. But I am nominated by the legislature and appointed by the Governor.

First, my colleagues and I would like to share with you a couple of key points about the process of looking at these amendments to the Single Audit Act that are being considered today. I can tell you that we are very pleased with the cooperation we have had from the Office of Management and Budget, from GAO, and also from committee staff. We think that at every occasion, we have had a full opportunity to share our points of view and our perspective, and we think that the amended version of the bill is an excellent vehicle which, after 10 years, is an appropriate time, we think, for change.

We think that the original Act was successful, and in fact, we look at it as meeting its objectives; but things have changed in the past decade, not the least of which has just been a change in the way that local and State governments manage themselves, but as well there have been changes even in the area of the amount of funds that are received by these various entities.

If I might just share with you an anecdote or two from what it was like prior to the 1984 Act, it must have been about 20 or 25 years ago, I recall an instance when I went to perform an audit at a particular entity, and when I arrived, the auditee, as we call them, or the subject of the audit, said, "We understand you have the power to do an audit here, but we do not have any room for you because we have three other Federal auditors and two other state auditors here, as well as our independent CPA, and we physically do not have a place for you to sit."

I think that while that might be an extreme, it does characterize to a certain degree what it was like when the audits that were being done were uncoordinated and oftentimes, as I consider them, ill-timed.

So the Single Audit Act came together, and further, I might just add that although there may have been five or six different auditors there, we were all looking at slightly different areas, although we looked at the same sets of books, because obviously, the expenditures were being processed by this one entity through its central system. So we were oftentimes basically competing for the same records.

But we did not really share our work. We did not have access—actually, at the time of that experience, I was with the General Accounting Office, so I did not have access to the records of the other Federal agencies nor did the state auditors who were doing the work.

So we did our work, and it was clearly duplicative of audit work that was being done by these other entities. What the 1984 Act did was bring together for the first time the concept of build-upon audits. That is to say, each entity that received a certain level of Federal funds would have an audit, and in our case in California, that is done by my office. And then, in the instance that a Federal agency or some other auditor needed more information than we were providing at the level of auditing we were doing, they would be able to do that, but they would do it in such a way as to build upon the work that we had already done. They would look at our working papers, they would determine and thus assure that they did not unnecessarily duplicate the work that had already gone on. It made a lot of sense, and it certainly received the audited entity from seeing all of these different auditors.

It was for those reasons that we embraced the Act and brought about the changes that were accomplished in 1984. There were problems, however, in the initial implementation. The Federal inspectors general, I believe—some of them; I should qualify that—believed that all of a sudden, they now controlled 50 separate state auditors and, likewise, local auditors and so forth, because the Act did mandate certain things be done. And as the State of California, we had early on decided to be one of the first states to assume the state-wide audit. We saw and we did have some initial problems dealing with the Federal sector, in terms of whether we were working with them or whether we were working for the state, and they could build upon our work.

So we did have some initial problems with the implementation. The Act was well enough drafted, however, that we could always look back to it, and we could say there is nowhere in here that says that we will do your beck and call. We are to do an audit meeting certain standards, and we will assure that that audit is accomplished, but we are not there to look at new areas for you or to do specific things at your direction.

So we worked that out, and in fact, over the ensuing years, as other states have come on line, they have not repeated the problems we saw in early 1985.

So, as I said, after 10 years, we think the original Act has become a success, and we think it is meeting its goals, but it is time to make some improvements.

Just two of the reasons that I think we should consider amending the Act and doing it this year are the change in the threshold—by raising that threshold to $300,000, we are going to relieve administrative burden and audit costs from literally hundreds, and perhaps thousands even in our state, of smaller local entities that will no longer have to meet these very rigorous and narrow standards that the Single Audit Act requires. Even in California's instance, on the largest end, there are changes proposed there which will relieve us of some of our administrative burden, and we do not think that it will in any way be a reduction in the amount of audit coverage that we are able to provide the Federal Government.

So that by changing the threshold even at the highest level, it will give some relief to the larger entities as well. That, coupled with an area that is called the risk-based audit approach, we think those two areas, amongst all the other changes, are worthy of this bill.

In that area, it is very simple—where can we get the most bang for the buck with the audit dollar. We ought to have the flexibility with the Federal Government to agree that some area has not been audited in years, and we ought to focus some resources there. That is our plan with the way we would use the concept of a risk-based audit. I think it makes absolute sense. It is the best use of the rare audit dollars that exist at the state level and certainly at the Federal level.

I have paraphrased my presentation, but again I want to emphasize that we are very pleased with OMB, GAO, and the Committee staff's continued acceptance of our concerns and approaches. The National State Auditors Association embraces the concept of these amendments. We have one or two small items that we want to share that we think will clarify or perhaps make the bill even a little better, but we are talking about just tweaking it at this point. We think it is a very excellent piece of work.

Chairman STEVENS. Good. We appreciate that, and we will look forward to those statements. I have heard from the Alaska State Auditor, also, and similar comments, and we are going to send him the statements and the bills, and we will be happy to have your written suggestions and consider them.

Mr. SJOBERG. Thank you.

Chairman STEVENS. Mr. Sheridan?

TESTIMONY OF TED SHERIDAN,[1] CHAIRMAN, COMMITTEE ON GOVERNMENT LIAISON, FINANCIAL EXECUTIVES INSTITUTE

Mr. SHERIDAN. My name is Ted Sheridan. I am president of Sheridan Management and chairman of the Financial Executives Institute's Committee on Government Liaison.

As you may know, FEI is a professional association of some 14,000 senior financial people, and I have logged 15 years myself as a CFO of major corporations.

I began my association with the CFO Act over a decade ago, working on a Grace Commission recommendation in that area. I testified before Senator Roth and before Senator Glenn during that period of time. And I think that at the 5-year mark, maybe we should do some midcourse corrections to take a look and see whether we are getting where the Act should be. And, rather than dwell on my prepared text, I am going to try to deal with only those things that have been brought up by the Senators this morning.

First of all, Chuck Bowsher mentioned the notion of an annual report, and I think that is one of the best ideas out there. Further, I think that this annual report should have the mission of the entity, the mission of the association, very well spelled out and should have all of those things that are necessary to understand what they need to do the job. It should then be forwarded to the various oversight committees and the appropriations committees—Senator Stevens on Defense, Senator Glenn, Senator Warner, John McCain; these people should have this document before them, knowing about the stewardship of these entities before they go forward in the authorization and also going on to appropriations. That would be our firm recommendation.

We would also hope that this would be the means by which—and this will go right to Senator Stevens' point—that we can create documents where the financial reports that we see will trace over into the budgetary process as we go forward so that they will have relevance not only for those people who are performing, but those that

[1] The prepared statement of Mr. Sheridan appears on page 78.

have to have the oversight and the appropriations responsibilities up here.

I further go on to talk about the notion that these entities should be able to do the job that Senator Glenn talked about inside of 5 years. I have been with John Hamre, and I have talked it over with him. I think he could do that job in 3 years—5 years at the outside—but there are some problems, and this relates to what Bill Phillips was talking about and what Senator Stevens asked about.

Some of the issues about getting a clean audit are clearly beyond the capability of those people who simply manage those departments. There are issues here that relate to—we talk about the EPA problems that our Air Force has. I have worked with Bob Hale, the assistant secretary there, on trying to handle some of these problems. When you try to create a liability, the notion of what a liability will be in the future, you are dealing with some very, very difficult concepts.

Now, FASAB has put down a ruling on this, but it is only about so big, and if you look at OMB, or if you look at GAO, the guidance given to the field simply is not there, and the folks have never done this before. So what we are saying is that we are going to have to go into this, looking at the audits in the following fashion. Rather than look at DOD as a huge entity that is so big, so complex, that you can never get your around it, you would go down to the legal entity basis—and FASAB provides for this—find those entities that we can audit, that are auditable, do them first and have a program of systematic audits. So there will be a scorecard that will say, OK, there are some issues out here that are going to be so difficult to deal with that we will put them into what, in the private sector, you call the "good bank" and "bad bank." You take some issues that you know are going to be difficult to work, and you put them off. In the meantime, you go to those entities that are part of the cutting-edge delivery of services and make sure that they are working. I would far rather know that air combat command is doing its job well, that it has its financial house in order, that try to account for some bombs that have been out in the desert for 20 or 30 years.

In doing this, we also want to talk about some technology, and Senator Stevens, you apparently shop at Wal-Mart quite a bit——

Chairman STEVENS. I have never been in one of their stores; I read about them, though.

Mr. SHERIDAN. There are things that can be done here from the point of view of technology, and I think that technology could be the answer to the problem. A lot of the problems are data entry problems. You have all of those clerks out in Columbus and Cleveland, shuffling pieces of paper. The technology exists now to use image scanning to get it into the system, or require that your vendors use electronic commerce, so that it is all in digital form. Then, with this, you have the integrity of the data going in, you utilize advanced telecommunications and relational databases to keep track of it; then you can do exactly what you want, and would also have the ability to have the unit level have the integrity of their system, so you can go down and put hour hand on somebody's shoulder and say, "You believe in these statements," but you could still have them roll up, and they could come out the top with the unified statement that you want.

I have talked to Bob Hale about this. He said, "Ted, I sign these CFO reports—I have to do it by law—but I cannot honestly account for all of these steps because we have lost track of the accountability." I think it would be important to bring that back.

Finally, in the area of trying to get the proper folks to work on the problem, from a financial executives' point of view, what we would propose is to offer a means by which we would help to bring people from the financial sector in, senior financial officers, to act as an advisory board for the 24 CFO Act companies and to be an independent audit group; bring some of the experience that we have had in downsizing and in rescheduling and in putting in new systems, to be the right-hand man of the Secretary and the CFO. And we are prepared to do that right now.

I am happy to answer any questions you have of me.

Chairman STEVENS. Thank you very much.

I should say for the record that I have no interest in Wal-Mart, and I believe there is not one near me, so I do not go there. But a friend of mine told me about it and said if you want to understand implementation of new technology, you have got to look at Wal-Mart, so I have done a lot of reading about Wal-Mart.

But I do think that one of the problems we have here is that it appears that we are getting to the point—if I understand what the three of you have said—where we have mandated compliance in the total accounting sense for the information that comes to us, we have required accountability, and perhaps that is what Mr. Phillips is saying, that there are some people who do not want to become accountable for the systems that they have to report.

Is that what you are saying, Mr. Sheridan? Are you saying what he is saying, that if the system does not work, it is because some people cannot verify the reports that come to them?

Mr. SHERIDAN. Exactly. They are not in a position because the accounting systems are so diverse, and many of them are coming up, getting financial information from so-called feeder systems that are not designed for financial reporting.

For instance, you will use a payroll system of a personnel system and try to strip off the information, so you lose the integrity of it. And I can see how somebody would say, "I just cannot attest to the fact that that is a good number," and in good conscience, he would like to be able to do that, but the system does not provide the opportunity to do that.

Chairman STEVENS. Now, Mr. Phillips, if I may, I understood your testimony to indicate that there are some people who did not think they would comply.

Mr. PHILLIPS. That is correct—not because they do not want to comply, but because they do not think they can comply. And that is a function of the things we have talked about here today—that is, we are being asked to have auditable financial statements. If the systems, if the business processes and procedures in place do not allow that to happen, I can put together financial statements for you, I can send a piece of paper forward, but whether those are auditable or not is in question. It is not an issue of wanting to; it is an issue of being able to.

Chairman STEVENS. Well, I do not want to belabor this, but how do I find that guy? How do I find a person who is not getting to the point where we can get a financially auditable statement?

I was just saying to staff, one of the things that compels Senators to pay up their bills around here is that when I was chairman of the Rules Committee, I said we are going to start posting your names if you do not pay your bills. You would be surprised how fast people pay their bills when they see their names on a wall.

Why wouldn't that work here? Why don't we find some way to put the names of the people who are not doing their work in the Congressional Record, so the world knows why we do not have an auditable statement? What I am telling you is that there is no sanction in this law. There is no sanction in the CFO law.

Mr. PHILLIPS. You have the names of the people in the CFOs, in the IGs, and in the secretaries of the agencies. Those are the people——

Chairman STEVENS. They are the ones who will not certify it because someone down below them will not give them the information; right?

Mr. PHILLIPS. That is right, and they are the ones who have responsibility for implementing these requirements. The challenge becomes sanctioning people who are trying to make something happen that cannot happen because the systems will not allow it to happen.

Chairman STEVENS. Well, I wonder if it is not back to what Senator Glenn asked—there are some people there who just do not want to put down the truth, who do not want to indicate that they have some unsolvable problems that they have been unwilling to attack.

Every once in a while, I find that someone in my office has an drawerful of correspondence that they are just unwilling to answer. We found one that was a couple of years old, as a matter of fact. That person is no longer there, but how do I find a way to tell other people who that person is so that they are not there? There is something holding up the system, in my opinion, if we do not get these reports the way the law requires.

Do you have any suggestions as to how we can get the information as to who is not performing?

Mr. PHILLIPS. Well, I think that you actually have a situation today that you did not have, let us say, 2 years ago or 3 years ago, just in terms of who the people are that are in those positions now.

In putting this survey together and working with the IGs and the CFOs, they were pretty forthright about what they want to do and what they are trying to accomplish. And I think that, probably better than any other time in recent history, we have people in place who want to make this happen. And I think that by working with them and by talking with them and having them come and talk to you, that those people are willing to be open about these kinds of things.

Chairman STEVENS. Mr. Sjoberg, I spent 4 years in the state legislature, and I think it must be a happier place now. I remember when the Federal auditors used to come into our legislative auditing agency; we thought we were doing the auditing, and suddenly, they thought they had the right to take over. It sounds to me like we worked that out.

Mr. SJOBERG. We did, and we do like the concept of doing the base audit ourselves and then, as the need arises for additional work to be done—we understand the Federal Government has a right to trace their dollars wherever they are spent—but our agencies then do not believe that they are being "over-audited" or that they are unnecessarily being burdened by having to gather information for more than one set of auditors in a given year.

Chairman STEVENS. Mr. Sheridan, do you have a relationship with Mr. Phillips company? What is your relationship to this company?

Mr. SHERIDAN. I have gotten to know his company through the work that I have done in telecommunications and in Indonesia, where I have done a lot of work. Their company asked me to make some comments on the CFO Act survey, and I have done that, and they were nice enough to put my picture in their magazine, as a matter of fact.

Chairman STEVENS. That is progress, I guess. But what I am trying to find out is whether the Financial Executives Institute—is that a corporate Financial Executives Institute?

Mr. SHERIDAN. The Financial Executives Institute is composed of 8,000 companies out there that have 14,000 people, mostly controllers and treasurers and chief financial officers. We are based on the chapter level in cities all over the country. Then we have so-called technical committees—a Committee on taxation, a Committee on Government reporting; we have one which is the Committee on Government liaison, where we are trying to get information from this city out to our chapters so that they can anticipate changes in various laws, tax regulations.

On the other hand, we also have offered our services to help as a resource to this community when asked. We testify when it is requested. We got to know Bob Hale because he found out about our work, and he called us up and said, "We need some help from the private sector." That is how I got to know him. I went over, and we talked about contingent liabilities and measurement things.

So that basically, we are resource and information pool for our members.

Chairman STEVENS. Well, that is good. I am glad to know about that resource. We might call on it when we get to reorganization.

Mr. SHERIDAN. We would be pleased to do that, sir.

Chairman STEVENS. My last question is to Mr. Phillips. You did this survey for whom?

Mr. PHILLIPS. We did it in conjunction with the Association of Government Accountants. We did it jointly because we felt there were tremendous opportunities for sharing progress and approaches to implementing the Act across agencies that we did not think was happening, and so we hoped that this would be a catalyst for best practices in benchmarking across Federal agencies.

Chairman STEVENS. I am most interested in it. Who paid for it?

Mr. PHILLIPS. Coopers & Lybrand paid for it.

Chairman STEVENS. You are a foundation, then?

Mr. PHILLIPS. No. We are a private partnership.

Chairman STEVENS. I find it very interesting. There are very distinct statistics. I want to read it—you gave it to us, didn't you?

Mr. PHILLIPS. Yes, sir. Your staff has a copy.

Chairman STEVENS. Thank you.

John?

Senator GLENN. Thank you, Mr. Chairman.

I was glad to have a copy of that survey, too. Could you discuss in a little more detail how the IGs and the CFOs differ, where their views converge and diverge, because we have heard that early on in this program, there was some problem with the CFOs and IGs working closely together. Maybe you have some insights on how that is working out now.

Mr. PHILLIPS. I think there is some natural conflict, just by the nature of the way they were designed. And in fact there is a third party in here that we talk about in the survey, and that is the GAO, because all three of them were asked a number of questions about who should do the financial audits, and they all had slightly different opinions on that.

I think that the issue with the groups boils down to the roles that they have played traditionally. When we asked the IGs what they saw as their role in auditing, they said that they felt that Congress wanted them to play more the investigative audit role. And that is important, and you need to have that, but in terms of the financial auditing, in terms of the traditional approach that firms take with financial auditing, it is much more of a partnership, working with the organization and trying to help them through their shortcomings.

That is a tough switch to make when the group that you are asking to do that has traditionally been the investigative arm.

Senator GLENN. Mr. Sheridan, Senator Brown has legislation to codify FASAB's accounting standards, basically. Two questions. One, how is the FASAB process working, in your view, and would it help to put it into law, or is that something that we do not really need?

Mr. SHERIDAN. Well, their process has been excellent. For the first time, we now have the foundation on which to build. In the private sector, we have something similar, the National Accounting Standards Board, which is independently monitored, and the entities, the corporations, voluntarily agree to do this. However, beyond that, the SEC has some codified aspects that are in law.

I think that to codify them as law would probably be a good idea because then it becomes the law of the land, but I would say that some of the issues in FASAB are judgmental, and it is awfully hard to codify judgmental issues like environmental cleanups and some of these contingent liabilities. But to the degree we can, I think that would be a good idea.

Senator GLENN. Yes. Some of my hesitancy is along that line on codifying these as Senator Brown would propose to do, in that it becomes less flexible once it is locked into statutory law, and there you are, and then you have to have a law to change it if you need any changes; where I think it is a little bit more flexible now and more adaptable—and maybe that is good, maybe it is bad; I do not know.

Mr. Sjoberg, your concerns on this are our concerns, too. The changes you suggest, the threshold change, we have in the proposal, and I think we give it perhaps even more flexibility than you indicated in your statement, in that we even take that 300,000 and say that that is even adjustable or, if they want to make a case for it, that they could even change that threshold; on exceptional cases, they could give a waiver there. So that makes it even a little more flexible.

Mr. SJOBERG. Yes, it does.

Senator GLENN. And the other, on the risk-based audit approach, I think we have that in there, also. So I think we are doing pretty much what you talked about, so I think we are moving along the same line here.

To all of you—in your observations about getting accountability from Government, personal accountability, is civil service an impediment to this?

[Pause.]

You know what I am thinking about. Mr. Sheridan, you would be a good one to take this on because you represent some of the private interests and how they manage their affairs, and if someone does not shape up, and they are not complying with the financial accountability standards that you have in a certain corporation, they are out—that is it, they are gone.

Civil service is a little more difficult. It is a little more difficult to fire people and get rid of them. Is that an impediment to more efficiency in Government?

Mr. SHERIDAN. I think we are seeing progress moving from the top down—the 24 CFOs we have who are political appointees, and their deputies, who by and large are career. We have a good cadre at that level, and I think it is moving down into the ranks.

Like in any corporation that restructures, there is going to be some pain, and there are going to be some people who no longer fit the bill. As we move into information technology, the people who are specialized paper-shufflers are going to, by attrition or other means, just go out of the system. So I think it is going to work its way over time, but I think the implementation of new and better, modernized systems is going to bring a different kind of person into financial management regimes.

Senator GLENN. Only very, very rarely in Government does someone pay personally for not performing. As the chairman pointed out, we have certain requirements here, and they are not going to be lived up to necessarily, and nobody will pay for that and probably nobody will get fired for that. In private industry, they well might. That threat is always there. So they have a lot more impetus or a lot more incentive to comply, perhaps.

I do not know whether this is a major factor in accountability in Government or not. If it is, we ought to correct it; if it is not, there is no need to beat a dead horse.

Mr. Sjoberg?

Mr. SJOBERG. Senator Glenn, 2½ years ago, my office went through a major reorganization, and we were essentially closed for 9 months. And when we reopened, we had to assume civil servant requirements of our State Constitution. We had for over 35 years been an exempt organization; that is to say, we could hire and fire at will. And since I manage under both systems, I might have a little different view than I would have had a few years back.

I can say that our new organization—because we have taken full advantage of all of the flexibility that is available through the civil service, including failing people on probation or actually removing people for cause—has assured that we maintain a certain level of accountability, and we have also instituted a pay-for-performance type of promotional system. All of those were within our constitutional boundaries.

The problem I see is the infrastructure of—we are only 2½ years old, so if we started out right, I think we will be fine. What happens to that agency that has been operating in such a way for 30 or 50 years? Therein lies the problem, and I think that what happens is that after a certain point in time, some individuals become entrenched, and by that entrenchment, they do feel as though they basically have a property right for their jobs, irrespective of how well they do it.

I think that at some point in civil service reform—and we have addressed that even in California—has to address the complacency that might occur in some civil servants after they have been there for 10 or 15 years, and to assure they maintain a certain level of competency. I think that with a change at that level, we will be able to assure that civil servants are not an impediment.

Senator GLENN. We know that efficiency saves money—obviously, that is accepted going in. It is difficult to quantify savings, where an organization is working more efficiently, but do you have any estimates of that? We just know that doing a single audit like you are talking about—you doing the threshold or basic audit, and then building on that; that is more efficient and is bound to save money. Have you been able to quantify any of that—I imagine it would be difficult to do—but either savings for the Federal Government in accomplishing their audit purposes and/or the State government doing theirs? Is there any way to put a dollar value to that?

Mr. SJOBERG. Well, we have tracked dollar savings for probably 15 or 20 years now in our office, and we do see currently about a $10 return for every dollar of audits——

Senator GLENN. So, a 10 to one return.

Mr. SJOBERG. Ten to one. It was $6 up until our reorganization, so something that we did streamlined it even more. So for the last 2½ years, it has been 10 to one.

Senator GLENN. How do you—it is late now, so I do not want to belabor this much further—but how do you come up with a 10 to one ratio—dollars spent on what to what?

Mr. SJOBERG. Well, we actually look at the improvements that have been made as a result of our recommendations; that is to say, track the implementation of recommendations——

Senator GLENN. Where a certain function is being performed, and you have suggested certain things, and that same function is being performed at lesser cost.

Mr. SJOBERG. Yes, so we have a before and after measure. And we have never even annualized some of these. I know that some of my audit colleagues have thought, well, if you make one change, and that would have been a problem that recurred for years and years and years, shouldn't you multiple that times some future date? Well, when we are using our 10 to one, we are using the one-year dollar cost recovery.

And that does not address, however, the qualitative benefits that come from audits, and that is just the improved services and things of that kind. So what I always like to do—and certainly, we are proud of a 10 to one return—but I use that in context and say that we also make recommendations that improve Government, improve accountability, which are not measurable in dollars and cents.

Senator GLENN. Well, I have been preaching for years that there are three parts to the budgeting process. One is revenues, another is expenditures, and the other is efficiency—and we never get around to efficiency, and that is the reason for CFO and all the rest of these things here. But it is awfully difficult to quantify.

If you have any studies like that that you have done, where you got your 10 to one, if you have a report on that that you could give to us, we would appreciate that for the Committee files, if you could give us a little guidance in that area.

Mr. SJOBERG. Sure; we will do that when we get back.

Senator GLENN. Do you have any similar things, Mr. Sheridan?

Mr. SHERIDAN. Yes, sir. In that regard, if we were to cut back through efficiency on either the outlays or the assets employed, 2.5 percent, you could balance the budget today. And to get a 2.5 percent reduction in the output, the costs, seems to me as a former CFO is a job that I could probably find a way to do that. And I think that is what we have got to do is put the encouragement there to the CFOs, actually, to put in measures of the efficiency of the delivery of the services, and then do cost accounting to figure out what it is costing to deliver that, and then we would know whether we could cut those costs or not. It is possible.

Senator GLENN. Yes. Mr. Phillips, do you have any comment?

Mr. PHILLIPS. Just to add to what Mr. Sheridan was saying, in the application of things like activity-based costing, which tells you what it costs to really do something as opposed to the way that we traditionally manage in terms of payroll lines, travel lines, travel lines, training lines, budget lines—those are the kinds of things that we need to get to so that we know what we are paying for. And the performance measures, focusing on our customers, will allow us to determine and will allow you to determine if in fact the agencies are doing what they are supposed to be doing.

Senator GLENN. Thank you, gentlemen. I appreciate it very much. You have been very patient. It has been a long morning here. I appreciate you being here.

Thank you, Mr. Chairman.

Chairman STEVENS. I will just close with this. Mr. Phillips, I have been leafing through your summary, and I was very interested to see that the senior financial managers ranked their program managers as the most important with regard to what they are assimilating in terms of their office, and that organizational leadership was second. The public was down, in terms of the top two categories, to only 10 percent. The Congress was at 28 percent. And I am not arguing with your figures, but where is the failure? Did you analyze that? The information really was designed for the public and for us who represent the public to try to determine the proficiency and efficiency and the necessity for the organization involved.

Have we failed somehow or another to get across why these reports are being prepared?

Mr. PHILLIPS. Well, I think you need—and we did some focus groups with them as part of this process—I think you need to really take a look at how those reports are used on an operational basis, on a day-to-day basis. And the CFOs do in fact see that the program managers, who need that financial information to make hopefully sound business decisions in their day-to-day operations, have that information.

Chairman STEVENS. You are assessing their function rather than the reports that we are talking about; right?

Mr. PHILLIPS. What I am saying is that in terms of a day-to-day use of this kind of information, it is the program managers, who have to execute major policies and major programs in the Government, who need to have this from an operational perspective on a day-to-day basis.

I do not think that if you asked the CFOs that they would say, well, yes, Congress is sort of a tertiary customer or that the American public is not really that important, which is what those numbers might tell you if you look at them very quickly.

But what they are responding to is the fact that, on a day-to-day basis, they are not interacting as a CFO with the American public; they are interacting with program managers and trying to in fact instill in them and with them fiscal responsibility.

So I think it is more of an emphasis on an operational basis as opposed to——

Chairman STEVENS. Well, the financial management community, which I would think would be OMB and CBO and GAO, were even lower than the other two. I am very interested in your report, and I am going to have to study it. It does indicate to me that we may need some greater emphasis in the targets. I think, in a period of declining discretionary spending, that these people had better understand that the information they are sending to us is going to determine whether they are at the high, middle, or low end of the totem pole as far as money when the cuts come, and that is what I thought they were for.

I do appreciate your long wait and your help, and I am delighted to know, Mr. Sheridan, that you are there. We will be calling on you next year, and maybe you, too, Mr. Phillips. Thank you very much for coming in.

This is going to be the last meeting of this committee this year. I will just announce that right now.

We stand adjourned.

[Whereupon, at 12:25 p.m., the Committee was adjourned.]

APPENDIX

PREPARED STATEMENT OF CHARLES A. BOWSHER

FINANCIAL MANAGEMENT

CONTINUED MOMENTUM ESSENTIAL TO ACHIEVE CFO ACT GOALS

Mr. Chairman and Members of the Committee:

I am very pleased to be here today to discuss the steady progress being made to improve financial management in the federal government through implementation of the Chief Financial Officers (CFO) Act of 1990. This landmark legislation was enacted 5 years ago thanks to the hard work of this Committee and its House counterpart. But, as I will outline today, a great deal more perseverance will be required to sustain the current momentum and successfully overcome decades of serious neglect in fundamental financial management operations and reporting methods.

To address these problems, the 1990 CFO Act spelled out an ambitious agenda of long overdue reforms. The CFO Act established a CFO structure in 24 major agencies and the Office of Management and Budget (OMB) to provide the necessary leadership and focus. To help instill greater accountability and fix pervasive and costly control breakdowns, financial statements were required to be prepared and audited, beginning with those for fiscal year 1991, for revolving and trust funds and commercial activities. For 10 agencies, audited financial statements were required as part of a pilot program to test this concept for an agency's entire operations. Moreover, the CFO Act set expectations for

—the deployment of modern systems to replace existing antiquated, often manual, processes;
—the development of better performance and cost measures; and
—the design of results-oriented reports on the government's financial condition and operating performance by integrating budget, accounting, and program information.

Important progress is being achieved to bring about these sweeping reforms and rectify the devastating legacy from inattention to financial management. OMB continues to play an important leadership role and a cadre of qualified CFOs are now in place and are seeking to make needed improvements. Similarly, the Inspectors General (IG) are embracing their new financial audit responsibilities. Additionally, much needed comprehensive accounting standards are nearing completion, and efforts are underway to further strengthen the quality of financial reporting. In short, financial management is finally becoming a top priority of federal managers.

Moreover, the regular preparation of financial statements and independent audit opinions required by the 1990 act are bringing greater clarity and understanding to the scope and depth of problems and needed solutions. These annual public report cards are also generating increased pressure to fix long-standing problems. The success of these efforts formed the basis for congressional action last year to pass the Government Management Reform Act of 1994, which expanded to all 24 CFO Act agencies the requirement for the preparation and audit of financial statements for their entire operations, beginning with those for fiscal year 1996. This essential expansion of the CFO Act's requirements provides a greater impetus for accelerated governmentwide implementation of financial management reform.

Also the 1994 act requires the preparation and audit of consolidated executive branch financial statements, beginning with those for fiscal year 1997. For the first time, the American public will have an annual report card on the results of current operations and the financial condition of its national government. This, in conjunction with the 24 CFO Act agencies' financial statements will set the foundation for the federal government to have the same kind of financial reporting as had already been required (1) by the securities laws for the private sector, partly in response to the stock market crash of 1929 and (2) by the Single Audit Act for state and local governments, driven in part by financial crises such as experienced by New York City in the early 1970s.

Making these reforms a reality in the federal government, however, remains a challenge for us all. Today, I want to focus on the four main implementation challenges to build upon the progress to date and put lasting improvements in place. They are:

—first, successfully implementing the expanded requirements for audited financial statements to improve the reliability of data for decision-making and strengthen the efficiency of financial operations and controls;
—second, continuing to build stronger financial management organizations by upgrading skill levels, enhancing training, and ensuring that CFOs possess all the necessary authorities within their agencies to achieve change;
—third, devising and applying more effective solutions to address difficult problems plaguing agencies' underlying financial systems; and
—fourth, designing comprehensive accountability reports to permit more thorough and objective assessments of agencies' performance and financial conditions, as well as to enhance the budget preparation and deliberation process.

In addition to achieving improvements in financial management at the federal level, this Committee has spearheaded greater oversight of hundreds of billions of dollars in federal spending at the state and local levels through the passage of the Single Audit Act in 1984. This act helps provide accountability for federal payments and instill fundamental elements of good financial management in state and local governments. The Committee in considering amendments to the act, which I will also address, to improve the effectiveness of the single audit process.

I want to commend the Committee for holding this hearing; sustained congressional attention to implementation of financial management legislation will be important in instilling greater accountability throughout the federal government and helping better control the cost of its operations. Thanks in large part to the legislative impetus of the expanded CFO Act and the Government Performance and Results Act—efforts led by this Committee—decisionmakers will ultimately have available unprecedented, reliable information on both the financial condition of programs and operations and the performance and costs of these activities.

Also, I will discuss the role this Committee could play in continuing to build on the foundation established through these laws for establishing a strong financial management organizational structure and revolutionizing the type and quality of financial information for decisionmaking. I believe this Committee, with the support of GAO, can work with the rest of the Congress to ensure that the wealth of new information to be generated through these statutory requirements will be provided to and used by appropriations, budget, and authorizing committees of the Congress and to bring the CFO Act's goals to fruition.

Data Reliability and Financial Operations are Beginning to Improve

To date, CFO Act financial audits have resulted in greater data reliability and improved financial operations. Under the expanded act, all 24 CFO Act agencies can begin to gain the benefits demonstrated by those agencies that have already successfully undergone full-scale financial audits. This is absolutely critical and will put the federal government on a par with the private sector and state and local governments, which have already made the necessary investment in financial management.

There is widespread consensus that the preparation and audit of financial statements has been the primary catalyst to increase the reliability of financial data and improve financial operations. During the past 5 years, due to the CFO Act's requirement, we have seen audit coverage substantially increase to almost half of the government's annual gross budget authority. Beginning with fiscal year 1996, due to the expanded CFO Act, audit coverage will expand to cover the entire operations of the 24 CFO Act agencies, which currently account for virtually all of the government's outlays.

Also, agencies are progressing in receiving unqualified audit opinions. In four cases, (the Social Security, General Services, and National Aeronautics and Space Administrations and the Nuclear Regulatory Commission) unqualified opinions were rendered on fiscal year 1994 financial statements covering agencies' entire operations. These agencies, which covered about 23 percent of the government's fiscal year 1994 outlays, have demonstrated that preparing auditable financial statements is possible and, with priority and emphasis, can be achieved by the remaining 20 CFO Act agencies as well.

In addition, there has been significantly greater commitment by the administration and agencies to effectively implement the CFO Act's expanded financial statement preparation and audit requirements. For example, OMB made it clear from the outset that it would not grant any waivers, although it has the authority to waive the requirement for fiscal years 1996 and 1997; thus, helping to ensure greater adherence to the statutory timetable. Also, OMB, Treasury, and GAO have been meeting with agency CFOs and IGs to build consensus, and we have generally seen a good commitment being given to preparing and auditing financial statements. For instance, some agencies, such as the Departments of Interior and Education, are on an accelerated schedule to having agencywide financial statements year before the act requires. Several CFOs and IGs have caveated their optimism, however, by the prospects that funding constraints could hold for dampening this momentum and hampering plans for meeting the act's fiscal year 1996 requirement.

It is essential that this time frame be met. As we have discussed in prior testimonies before the Congress, audited financial statements have provided significantly more accurate and useful information on the government's financial status and its operations.[1] Further, CFO Act financial audits have provided a greater understanding of the extent and nature of the financial control and systems problems facing the government, and a better appreciation for the limited extent to which the Congress and program managers can rely on the information they receive. Effective implementation of the CFO Act's expanded requirement for audited financial information is essential for more informed decision-making and better accountability in virtually every major aspect of the government's operations, as the following examples illustrate.

Improving Revenue Collection Operations Essential to Fund the Government

In fiscal year 1994, the federal government collected a reported over $1.3 trillion in revenue, primarily from individual and corporate income taxes and import duties, fines, and fees. Reliable financial data are necessary to ensure that the government assesses and collects more of the revenue that is due from these sources. This, however, is not yet the case, as shown by our financial audits at the Internal Revenue Service (IRS) and the U.S. Customs Service.

The Internal Revenue Service

The process of preparing and auditing financial statements for the government's primary revenue collection agency has surfaced significant problems affecting its operations and credibility. For example, through these audits, it came to light during our first audit of IRS's financial statements—those for fiscal year 1992—that IRS could not

—verify or reconcile its $1.3 trillion in reported revenues to its accounting records;
—substantiate amounts for various types of taxes reported, such as social security, income, and excise taxes, although the amounts of these taxes are to be separately maintained;
—reconcile its cash accounts with Treasury's;
—substantiate its billions of dollars of gross and net accounts receivables, and
—adequately account for its annual operating funds.

To its credit, IRS has made a commitment to institute changes. Through the strong support of the Commissioner, the agency has made important strides to address its far-reaching financial management problems. IRS successfully implemented a new administrative accounting system in fiscal year 1993 that can better account for its more than $7 billion in annual operating funds. It entered into an agreement with the Department of Agriculture's National Finance Center and now has control over its $5 billion payroll operations, which was lacking at the time of our first audit. It has taken physical inventories of its equipment and is beginning to get full control over these assets. IRS has ongoing efforts, including the use of outside contractors, to resolve its cash reconciliation problems and to strengthen its internal controls over payments.

Finally, although necessary systems changes to bring revenue accounting up to reasonable expectations have not been completed, better estimates of collectible delinquent taxes are now being developed as part of the financial statement preparation process so that the Congress will have the information needed to better gauge potential collectibility and to ask questions as to why amounts are not collectible. For example, the audit for fiscal year 1992 disclosed that IRS had $65 billion in de-

[1] These testimonies are listed in attachment I.

linquent taxes outstanding, not the $110 billion IRS reported and, of the $65 billion, only $19 billion was estimated to be collectible. This type of data would provide a more reliable basis than has been available in the past on the merits of adding collection personnel.

The future holds even greater potential. First, IRS is beginning to address the systems issues that will enable it to reliably show by type of tax how much has been actually received and who pays the tax. For example, excise taxes, such as petroleum companies and chemical manufacturers, among others, pay to fund environmental cleanup activities, are to be segregated by type and are used to achieve specific policy goals. But our financial audit showed that IRS's accounting system does not have this capability. Consequently, whether it be the Superfund Trust Fund or the Highway Trust Fund, a fund may be receiving more or less than it is due.

Social security taxes are somewhat different in concept but the problem is the same. Under law, the Social Security Administration (SSA) receives social security taxes based on wage information reported by employers to IRS even if the taxes are ultimately not paid. This results in amounts going to the Social Security Fund from other tax sources, and while the IRS knows that there is a discrepancy, it cannot yet identify that amount so that decisionmakers will know the cost of this policy. As a result of the financial audit, IRS is now working to address these problems.

Future systems changes should also result in extending the application of accrual accounting to the tax revenue stream so that IRS and the Congress will have somewhat better information about the taxes IRS should be collecting. Further, because the CFO Act calls for the development of better cost and performance data, IRS will have an opportunity to better justify and manage tax compliance initiatives. For example, over the years, questions have been raised over the amount of revenue to be generated from adding revenue agents or initiating special compliance initiatives. Such questions can only be conclusively answered by improving the basic reliability of IRS's underlying data.

The U.S. Customs Service

Financial audits of the Customs Service, the government's second most important revenue collector, revealed problems similar to those at IRS. These problems impaired Customs' ability to effectively ensure that carriers, importers, and their agents complied with laws intended to ensure fair trade practices and protect the American people from unsafe and illegal imported goods. Further, these audits found that Customs did not

—adequately ensure that all goods imported into the United States were properly identified and that the related duties, taxes, and fees on imports, reported to be over $21 billion for fiscal year 1993, were properly assessed and collected;
—have adequate controls to detect and prevent excessive or duplicate refund payments;
—have adequate accountability over tons of illegal drugs and millions of dollars of cash and property seized or used in its enforcement efforts; and
—have adequate controls over the use and reporting of its operating funds.

The Commissioner of Customs has expressed a strong commitment to resolve these problems and recognizes that a significant and sustained effort by Customs' management will be required. Acting on this commitment, Customs has developed and tested nationwide, a new program to reliably measure the trade community's compliance with trade laws. This program is expected to achieve better overall compliance with trade laws and tighter controls to ensure that the government receives all of the import taxes, duties, and fees to which it is entitled. This information will also help Customs ensure that it is making the best use of its limited inspection and audit resources.

Moreover, Customs has developed and applied methodologies for more accurately reporting its collectible accounts receivable. It also reorganized its debt collection unit, formalized its collection procedures, and aggressively pursued collection of old receivables. According to Customs, this effort resulted in collections of over $35 million. Customs also began conducting nationwide physical inventories of its seized assets to improve the safeguards over this property and has taken steps, such as implementing basic reconciliations of records, to ensure more adequate control over the use and reporting of its operating funds.

Providing Accountability for National Defense Expenditures

The Department of Defense (DOD) must have accurate financial information and internal controls to manage the Department's vast resources—over $1 trillion in assets, 3 million military and civilian personnel, and a budget of over $250 billion for fiscal year 1995. Effective financial management is critical to assuring that these resources are productively employed in meeting our nation's defense objectives.

Unfortunately, DOD does not have effective financial management operations and the seriousness of its financial management problems caused us to add it to our high-risk list. No single military service or major component has been able to withstand the scrutiny of a financial statement audit. This failure has serious implications. Good financial management runs deeper than the ability to develop accurate financial records. It is being able to (1) provide managers with visibility and control over inventories, (2) project material needs, and (3) effectively balance scarce resources with critical needs.

The CFO Act audits have served as an important catalyst for identifying and focusing management attention on the full extent and scope of the financial problems facing the Department. Since 1990, we and the DOD auditors have made over 350 recommendations to help resolve the financial management weaknesses identified throughout the Department. These audits have consistently identified fundamental deficiencies in DOD's financial operations. For example, these audit have served to highlight that:

—As of August 1995, DOD problem disbursements—those for which the Department can not match a disbursement with a related obligation—were reported to be $28 billion—and DOD continues to make hundreds of millions of dollars in overpayments to its contractors. As a result, DOD can not ensure that it does not spend more than it is authorized—a basic fund control responsibility.

—DOD does not have adequate records or controls over the multibillion dollar investment in government furnished property and equipment.

—DOD has failed to properly report billions of dollars in potential future liabilities, such as environmental cleanup costs.

Further, beginning for fiscal year 1996, the Navy general fund operations will be subject to audit. We reviewed the Navy's fiscal year 1994 financial reports as a measure of the Navy's current ability to prepare reliable financial statements. In our pending report, we conclude that, to an even greater extent than the other military services, the Navy is plagued by troublesome financial management deficiencies involving tens of billions of dollars.

DOD has recognized the seriousness of its financial management problems and the need to take action. Secretary Perry and Comptroller Hamre have been candid in their assessments of the status of current processes and practices. Further, the Department's financial reform blueprint—presented in February 1995—offers a good perspective of the corrective actions which must be taken. We believe this plan represents an important first step in committing DOD to real action.

As we testified earlier this year, however, very serious management challenges face the Department as it moves to make the blueprint a reality.[2] We recommended that DOD determine what skills are required to ensure that the plan is developed and implemented and to establish an independent, outside board of experts to provide counsel, oversight, and perspective to reform efforts.

We are also concerned about the pace of needed improvements at DOD. According to a recent DOD IG report, DOD's development of new accounting systems will not be completed until the end of fiscal year 1998 and, consequently, DOD's IG will not be able to render audit opinions on any of the military services' general fund operations until March 2000 at the earliest.

As we testified last month, given the serious and pervasive nature of DOD's financial management problems, and the need for more immediate progress, the Department needs to consider additional steps to (1) establish a skilled financial management workforce, (2) ensure that financial management systems are capable of producing accurate data, and (3) build an effective financial management organization structure with clear accountability.[3] We will continue to review more detailed implementation plans intended to carry out DOD's blueprint—including assessments of DOD's strategy and timing of proposed actions—and to work with DOD on implementing recommended improvements.

Instituting Better Management of Federal Lending Programs

The federal government is the nation's largest single source of credit. It lends or guarantees hundreds of billions of dollars of loans for a wide variety of programs,

[2] *Financial Management: Challenges Confront DOD's Reform Initiatives* (GAO/T-AIMD-95-143, May 16, 1995) and *Financial Management: Challenges Confront DOD's Reform Initiatives* (GAO/T-AIMD-95-146, May 23, 1995).

[3] *Financial Management: Challenges Facing DOD in Meeting the Goals of the Chief Financial Officers Act* (GAO/T-AIMD-96-1, November 14, 1995).

such as housing, farming, education, and small business. At September 30, 1994, the government reported (1) $241 billion in nontax receivables, of which $49 billion, or over 20 percent, was reported to be delinquent and (2) $694 billion in guarantees of outstanding loans for which it was contingently liable. There are four principal credit agencies: the Department of Agriculture, with 56 percent of the loans; the Department of Housing and Urban Development (HUD), with 11 percent of the loans and 55 percent of the guarantees; the Department of Education, with 7 percent of the loans and 11 percent of the guarantees; and the Department of Veterans Affairs, with 23 percent of the guarantees.

We have long been concerned about the quality and reliability of financial information on credit programs. Our audits, as well as those by the IGs, have consistently disclosed serious weaknesses in agency systems that account for and control receivables, and three of the lending programs—(1) farm loans, (2) student financial aid, and (3) housing guarantees—are on our high-risk list. Agency managers need accurate and reliable information on a day-to-day basis to effectively manage multibillion dollar loan and loan guarantee portfolios and to determine the value and collectibility of debts owed the government. For example, audits have disclosed weaknesses in agency approaches to estimating losses on these loans and, in some cases, have resulted in significant adjustments to the recorded loss reserves.

—In response to problems identified in the Federal Housing Administration's (FHA) fiscal year 1991 financial statement audit and to prepare for the fiscal year 1992 audit, FHA's management initiated a special study to better estimate loan loss reserves. As a result, in fiscal year 1992, FHA's loan loss reserves for the multifamily General Insurance (GI) and the Special Risk Insurance (SRI) funds increased by $6.4 billion. The GI reserve increased from $5.8 billion to $10.6 billion and the SRI reserve increased from $156 million to almost $1.9 billion.

—Financial audits of the Federal Family Education Loan Program identified that Education's estimates of the cost to the government of loan guarantees, estimated at $15.2 billion as of September 30, 1994, were derived using unreliable data. Education is now working more closely with the guaranty agencies to understand and resolve some of the student loan data errors.

As a result of these and other on-going financial audits, there now exists a clearer picture of the government's performance and loss estimates for lending programs. The loss estimates will become more accurate as agencies gain experience in implementing the Credit Reform Act of 1990 and the related accounting standard for direct loans and loan guarantees developed by the Federal Accounting Standards Advisory Board (FASAB). These efforts and the ongoing audit process should result in appropriate systems and methodologies being implemented to provide critical program cost and budget information.

Bringing Other Key Federal Investments and Activities Under Financial Audit Scrutiny

The expansion of the CFO Act's financial statement preparation and audit requirement will bring a significant amount of the federal budget under examination for the first time. For example, the first full audit of almost $300 billion of Medicare and Medicaid expenditures, or about 19 percent of the federal government's expenditures, will be performed. This will be especially important, given the role of Medicare and Medicaid spending in driving the growth of federal expenditures in the foreseeable future.

Moreover, some health care experts have estimated that as much as 10 percent of national health care spending is lost to waste, fraud, and abuse. Also, we and others have reported many prior problems with these programs, and limited financial audits to date have shown a lack of detailed supporting records. For example, the Health Care Financing Administration's fiscal year 1994 balance sheet audit disclosed inadequate or no documentation supporting over $100 million of Medicare receivables under contractor supervision, making collectibility questionable.

A full financial audit of these expenditures will provide a much better understanding of the reliability of reported Medicare and Medicaid payments, control weaknesses that permit waste, fraud, and abuse to occur and needed corrective actions, and the impact of noted problems on program operations.

Another significant area to be audited is the federal government's substantial environmental cleanup costs relating to federal facilities that were contaminated with nuclear materials or other hazardous substances. OMB estimated in October 1995 that the federal government's known environmental cleanup costs could range from $200 billion to $400 billion in the years ahead. The agencies included in this estimate are the Departments of Energy, Defense, Interior, and Agriculture and NASA.

The full magnitude of the government's environmental cleanup liability is unknown. For example, $200 billion to $350 billion of the above amount was estimated for Energy alone; however, Energy's estimate excludes certain costs, such as costs related to those items for which technological solutions do not currently exist, such as most groundwater contamination.

The agencywide audits conducted under the expanded CFO Act requirements will provide an indication of the reasonableness of current agency estimates. In addition, financial statement disclosures will provide information on the nature, location, and magnitude of the federal government's overall exposure for environmental cleanup.

In addition to these major investments, there are other key federal investments that will come under scrutiny as well. We are concerned, however, that scrutiny for some of these investments may not occur soon enough because a few agencies may slip in meeting the CFO Act's time schedule. For example:

—The Federal Emergency Management Agency (FEMA), which in fiscal year 1992 through fiscal year 1994 made $7 billion in relief payments, will not be ready to have its Disaster Relief Fund's financial records and reports audited within the next year. The fund's accounting records contain inaccurate data that have never been reconciled to supporting records, including unliquidated obligations of over $4 billion for disasters that date back to FEMA's inception in 1979. To prepare for the audit, FEMA has, with contractor help, begun the necessary reconciliation. FEMA has stated that it plans to have agencywide audited financial statements beginning with fiscal year 1998.

—The Department of Transportation (DOT) had over $47 billion in fiscal year 1994 gross budget authority and is accountable for important aspects of ensuring the development and safety of the nation's highways, railroads, and airways, including those administered by the Federal Highway Administration, the Federal Aviation Administration, and the Coast Guard. DOT has not yet prepared agencywide financial statements and does not plan to do so for fiscal year 1995. Based on DOT's progress to date, without additional impetus, it is uncertain as to whether the Department will be ready to prepare reliable consolidated agencywide financial statements within the statutory time frame.

—Under the requirements of the CFO Act, the Department of Justice (DOJ), which does not have many trust or revolving funds or commercial functions and was not part of the pilot program, was not required to audit many of its significant operations. Of its $13.5 billion in gross budget authority, only 12 percent, or $1.6 billion was subjected to audit. DOJ's major bureaus, such as the Federal Bureau of Investigation, Drug Enforcement Administration, Immigration and Naturalization Service, U.S. Attorneys Office, and Marshals Service have not been audited, nor have financial statements been prepared for these entities. DOJ is the only department that has requested a waiver from the preparation and audit of departmentwide financial statements for fiscal year 1996 under the expanded CFO Act requirements. The Department has cited as the basis for its request the lack of experienced staff to prepare financial statements and the lack of funds to contract for the audits. We believe DOJ needs to make a commitment to the audited financial statement requirements and view this as a priority because of both technical and cultural challenges that must be overcome.

Addressing and Fixing Control Weaknesses

Financial audits are also continuing to find and propose corrective actions to resolve long-standing material internal control weaknesses at the agencies under audit. These audits also continued to provide a much needed discipline in pinpointing operational inefficiencies and weaknesses, highlighting gaps in effectively safeguarding the government's assets, and preventing possible illegal acts.

Financial audits, for instance, identified information security weaknesses that increased the risk that sensitive and critical computerized data and computer programs will be inappropriately modified, disclosed, or destroyed. For example:

—IRS continued to lack sufficient safeguards to prevent or detect unauthorized browsing of confidential taxpayer records;

—student loan data maintained by Education could have been modified for fraudulent purposes because users had the ability to override controls designed to prevent such actions;

—FHA had continuing weaknesses in systems, including those that process sensitive cash receipt and disbursement transactions;

—at the Customs Service, thousands of users had inappropriate access to critically sensitive programs and data files; and

—the Navy had significant weaknesses involving access to financial data and the adequacy of computer center plans for recovery if service is interrupted.

Further, financial statement audits have continued to identify potential and actual dollar savings. These savings include the recovery of millions of dollars in overpayments to DOD contractors, the collection of receivables, the recoupment of payments incorrectly made to government intermediaries and employees, and reductions in the cost of operations that are excessive.

Further, financial audits are disclosing areas where the government may be paying more than it should or may not be collecting all that it should. For example:

—Education did not have systems or procedures in place to ensure that individual billing reports submitted by guaranty agencies and lenders were reasonable. For fiscal year 1994, these billings paid were estimated to be $2.5 billion.

—The Coast Guard could not provide detailed supporting records for almost $100 million of accounts receivable reported for the Oil Spill Liability Trust Fund and the associated $65 million estimate for uncollectible accounts.

Financial audits have also shown that agencies often do not follow rudimentary bookkeeping practices, such as reconciling their accounting records with Treasury accounts or their own subsidiary ledgers. These audits have identified hundreds of billions of dollars of accounting errors—mistakes and omissions that can render information provided to managers and the Congress virtually useless. This situation could be much improved if more rigor were applied in following existing policies and procedures.

Preparing and Auditing Governmentwide Financial Statements

Beginning with those for fiscal year 1997, Treasury will prepare financial statements for the executive branch as a whole, and we will audit these statements. For the first time, the American public will have an annual report card on the results of current operations and the financial condition of its national government. I am most pleased that this requirement has finally become a reality. My hope is that the requirement for audited financial statements would be extended to the legislative and judicial branches so that these could be included in audited governmentwide consolidated financial reports to the American taxpayers. I am also pleased that the Federal Reserve has contracted for financial audits over the next 5 years. My hope is that other independent agencies of the government would do likewise.

As the consolidated executive branch statements evolve and when the quality of the underlying data can withstand the scrutiny of an independent audit, they will not only be useful for decisionmakers but will help engender public confidence that the federal government can be an effective financial steward, fully accountable for the use of tax dollars. These statements should provide a clear picture of the financial demands and commitments of the federal government, the available resources, the execution of the budget, and the results, both financial and performance, of current operations.

We are working closely with OMB, Treasury, the agency CFOs, and the IGs. We have formed a series of task forces to address accounting and auditing issues and are actively supporting the work of FASAB. This is a tremendous undertaking and will require all parties to work together. For our part, we are going to

—focus on performing the IRS financial statement audit for the fourth year and conducting the first-ever financial statement audit for the Bureau of Public Debt, which accounts for more than $3.4 trillion of federal debt held by the public and the related annual interest payments;

—undertake selective work at selected major agencies involving, for example, SSA's 75-year actuarial projections, DOD's mission assets (valued at over $1 trillion), the almost $200 billion Medicare program, and the almost $100 billion Medicaid program, and at these agencies, we will coordinate our efforts with the IGs; and

—work cooperatively with the IGs at the 24 CFO Act agencies as they audit other major key accounts.

This will be a major challenge. We are very much depending on the 24 CFO Act agency IGs to do their individual audits, and are concerned about the extent to which budget constraints may affect their ability to perform those audits properly and timely. I am also concerned, that GAO's downsizing has left us short of the accounting and financial systems expertise needed in 1997 to conduct the consolidated executive branch financial statement audit. Even though I have reassigned personnel within GAO to the maximum extent possible, we are still short about 100 to 150 people who possess the technical skills we need to do the job. I expect this problem to be even further exacerbated as we experience additional attrition in these areas throughout 1996. We plan to consult with the Congress about this problem in the context of our fiscal year 1997 budget submission.

CONTINUING TO BUILD EFFECTIVE FINANCIAL MANAGEMENT ORGANIZATIONS

The leadership envisioned by the CFO Act is beginning to take root. In general, we have found that OMB's Deputy Director for Management and Controller and the agency CFOs and Deputy CFOs meet the qualifications outlined by the CFO Act. Also, the CFOs are active in their agencies and as a group through the CFO Council, which the act created, to provide the leadership foundation necessary to effectively carry out their responsibilities.

CFO Act agencies, however, need to ensure that CFOs possess all the necessary authorities within their agencies to achieve change. For instance, because of the interdependency of the budget and accounting functions, many agencies have included both budget formulation and execution functions under the CFO's authority. However, at a few agencies, such as the Department of Agriculture, HUD, and the Agency for International Development, CFOs do not have a full range of budget responsibilities. HUD's CFO, for instance, maintains records of, and provides HUD's budget office with, information on obligations and unexpended balances but is not involved in formulating the budget or allocating and reallocating funds throughout the year. At Education and Labor, CFOs have responsibility for budget execution but not for budget formulation. We believe that each CFO Act agency should recognize that both these functions can best be integrated with the agency's other financial activities by delegating responsibility for them to the CFO.

Also, at many CFO Act agencies, financial management responsibility rests with the CFO but is carried out by the financial leaders at the agencies' components, which can create problems. For instance, we recently reported that the Department of Agriculture's CFO has neither the authority within the Department nor the mechanism to enforce compliance with its financial standards.[4] To overcome this kind of situation, we believe it is important for CFOs to have a strong role in and authority over component financial management matters.

Additionally, some CFOs have responsibility for operational functions, such as procurement and grants management, in addition to those directly related to agency financial management. While functions such as these can provide opportunities for much needed integration of different functional areas, they also have the potential to distract the CFOs from concentrating on financial management issues throughout the agencies.

Another serious problem the CFOs face in building an effective supporting structure is attracting and retaining well qualified financial management personnel and working to upgrade staff skills in a constrained budget environment. Financial audits have shown with greater clarity the extent and nature of the government's financial management personnel shortages and the importance of overcoming them.

These audits have consistently disclosed agencies having extraordinary financial management problems in even the fundamental areas of making reconciliations, documenting adjustments, ensuring that inventories are taken, and making supervisory reviews of accounts and transactions. Weaknesses such as these lead us to believe that fundamental skill levels and training issues must be addressed quickly.

Moreover, implementing the CFO Act's objective of upgrading financial operations, such as developing performance measurement systems and integrating budget and accounting data, will require significantly enhanced staff skills. Focusing on these areas is difficult when agencies' basic financial and control weaknesses remain unchecked. Top managers are, however, beginning to get a sense of the extraordinary effort that will be needed to upgrade financial management organizations and to fix known problems.

In this regard, OMB's July 1995 *Federal Financial Management Status Report and Five-Year Plan* addresses the need to develop a quality financial management workforce by implementing methods to assist agencies in recruiting and retaining qualified financial management personnel. CFOs, though, have a significant challenge in building effective organizations to meet the CFO Act's challenges.

To help in this area, in June 1992, the Association of Government Accountants made 30 recommendations covering all facets of the financial personnel challenge, from recruiting talented staff to reducing turnover. The CFO Council's Human Resources Committee is working to implement these strategies through such activities as coordinating efforts to provide low-cost, effective financial management training

---

[4] *USDA Financial Systems: Additional Actions Needed to Resolve Major Problems* (GAO/AIMD-95-222, September 29, 1995).

and developing a plan for establishing core competencies and standards for all CFO-related positions.[5]

Investments must be made in training to ensure that financial management personnel increase their professional skills to keep pace with emerging technology and developments in financial management. However, financial management training is often a neglected aspect of ensuring high-quality financial operations. In our discussions with the 24 CFO Act agencies, most said they had not established formal training programs to enhance the skills and knowledge of financial management staff.

However, some agencies have acted. The Department of Energy, for example, has established a training program for financial managers that all of its CFO offices are required to implement and that is based on employees' individual development plans. Also, the Department of Education requires its financial personnel to complete 40 hours of continuing professional education annually.

We have called for financial management personnel to be required to participate in a minimum amount of continuing professional education.[6] Government auditors are required to attend 80 hours of continuing professional education every 2 years, and this requirement has helped enhance audit quality and professionalism.

We believe, though, that upgrading and training financial management staff requires much greater short-term attention to identify more specifically the extent of the skills gap and how it can be most effectively narrowed or closed. We plan to study this area in more depth in the coming months and will report the results to the Committee.

In this regard, the Committee can be of assistance by challenging the CFOs to clearly identify financial management skill shortages in terms of personnel needs to effectively achieve the CFO Act's financial management objectives. Further, the Committee can encourage agencies to get the resources and financial management talent needed to make the needed improvements.

Building Sound Financial Management Systems

Seriously inadequate financial management systems are currently the greatest barrier to timely and meaningful financial reporting. Agency systems are old and do not meet users' needs. In March 1995, OMB reported that 39 percent of agency systems were originally implemented over 10 years ago; 53 percent need to be replaced or upgraded within the next 5 years.

The CFO Council has designated financial management systems as its number one priority. The need for this emphasis is underscored by the results of self-assessments by the 24 CFO Act agencies, which showed that most agency systems are not capable of readily producing annual financial statements and are not in compliance with current system standards. Equally as important, as a result, managers do not have reliable, timely financial data throughout the year to help manage effectively.

The poor condition of agency financial systems is a symptom of a much broader issue—the federal government's overall inability to effectively manage investments in information technology (IT). Many projects have been poorly managed, cost much more than anticipated, and have not provided intended benefits.

There is a growing recognition that fundamental information technology management problems need to be addressed, and a number of initiatives are underway to do this. For example, our May 1994 executive guide[7] on the best information management practices of leading organizations has been enthusiastically received, and several agencies are actively attempting to implement its tenets. We testified before this Committee on the key practices outlined in this guide.[8]

Also, we have developed several tools to assist agencies in taking a strategic view of their information resource management practices and maximizing their IT investments. Our *Strategic Information Management (SIM) Self-Assessment Toolkit*,[9] for example, has been used by several agencies, including IRS and HUD, and has already resulted in several million dollars in savings. In August 1995, we issued an exposure draft of our *Business Process Reengineering Assessment Guide*, which is currently being pilot tested at several agencies. Additionally, we have worked with

[5] *Framework for Core Competencies for Financial Management Personnel in the Federal Government* (August 1995 (Draft)).

[6] *Financial Management Issues* (GAO/OCG–93–4TR, December 1992).

[7] *Executive Guide: Improving Mission Performance Through Strategic Information Management and Technology* (GAO/AIMD–94–115, May 1994).

[8] *Government Reform: Using Reengineering and Technology to Improve Government Performance* (GAO/T–OCG–95–2, February 2, 1995).

[9] *Strategic Information Management (SIM) Self-Assessment Toolkit* (Version 1.0, October 1994 Exposure Draft).

OMB in finalizing *Evaluating Information Technology Investments: A Practical Guide*, which will provide agency managers a systematic and objective means of assessing the risk and maximizing the return associated with planned IT investments.

Further, the Congress is taking steps to improve federal IT management. Earlier this year, the Congress amended the Paperwork Reduction Act, which the President signed into law on May 22, 1995. The amendments should improve the management of IT resources and institute stronger controls over investments. Other legislative proposals to strengthen leadership and accountability are being considered, including establishing Chief Information Officers and changing system planning and acquisition practices.

There are also improvement efforts underway specifically aimed at financial systems. For example, in January 1995, the Joint Financial Management Improvement Program (JFMIP) published a model for establishing and maintaining integrated financial management systems. This document, entitled *Framework for Federal Financial Management Systems*, is an important step in providing needed guidance.

Additionally, OMB's July 1995 *Federal Financial Management Status Report and Five-Year Plan* sets out broad objectives, tasks, and milestones to help improve systems. The plan, for example, addresses making better use of off-the-shelf technology, cross servicing, and outsourcing. Overall, OMB's objectives have provided the right emphasis and priority for financial systems improvements. OMB and the CFO Act agencies must now focus on specific implementing policies and strategies.

To help these efforts, we are preparing a methodology for reviewing financial management systems. This methodology also could provide a starting point to help agencies develop systems requirements for building integrated information systems to support their missions, operations, and governmentwide reporting requirements. We plan to work with OMB and the CFO Council to move in this direction and will report the results to the Committee next spring.

Also, since the benefits of long-term efforts to improve agency systems often require years to realize, agencies need to make their existing systems work better in the interim. An important aspect of this is to ensure the validity of existing data and implement the routine controls needed to keep these data reliable, such as reconciliations to identify and resolve discrepancies. Such efforts will improve data reliability and help ensure that information transferred to new systems is accurate.

EFFORTS TO STRENGTHEN ACCOUNTABILITY REPORTING WILL GREATLY AID DECISIONMAKERS

One of the CFO Act's primary goals is to enhance the reporting of reliable financial and performance data that are useful and understandable to program managers and congressional decisionmakers. Prior to its enactment, despite good intentions and past efforts to improve financial management systems, the government was not using timely, reliable, and comprehensive financial information when making decisions having a tremendous impact on the American public. The first important step was taken with the CFO Act requirement for the preparation and audit of financial reports to achieve basic data reliability. Now, at least we will know when data are reliable and when they are not.

The next steps, which build on the foundation laid by the CFO Act, will further enhance the usefulness of accountability reporting to decisionmakers by integrating performance measures into the reports and developing reports more specifically tailored to the government's needs. They include the efforts of the Federal Accounting Standards Advisory Board (FASAB) to develop accounting standards and OMB's efforts to implement the Government Performance and Results Act (GPRA) and to develop streamlined Accountability Reports.

FASAB Efforts

As you may know, FASAB was established in October 1990 by the Secretary of the Treasury, the Director of OMB, and myself to consider and recommend accounting principles for the federal government. The nine-member Board is comprised of representatives from the three principals, the Congressional Budget Office, the Department of Defense, one civilian agency (presently from Energy), and three representatives from the private sector, including the Chairman, former Comptroller General Elmer B. Staats. FASAB publishes recommended accounting standards after considering the financial and budgetary information needs of the Congress, executive agencies, other users of federal financial information and comments from the public. OMB, Treasury and GAO then decide whether to adopt the recommended standards; if they do, the standard is published by GAO and OMB and becomes effective.

Early next year, FASAB will complete the federal government's first set of comprehensive accounting standards developed under this consensus approach, which has worked well. While the development of accounting standards as envisioned by FASAB and its three principals is very important to strengthening accountability, the benefits will come from their full implementation.

It is our understanding that Senator Brown plans to introduce legislation that would establish in law the FASAB process, which at this time, is operating under a memorandum of understanding. Among the purposes cited in the legislation is to provide for uniform adoption and application of accounting standards across government and the establishment of systems that meet the requirements of the CFO Act. The legislation being considered calls for each federal agency to give priority to funding and provide sufficient resources to implement the act.

Further, the proposed legislation would require an agency's CFO Act auditor to report whether the agency's financial management system complies substantially with the FASAB accounting standards and other financial management system requirements. We understand that Senator Brown's proposal will also include mechanisms to highlight an agency's compliance problem to the Congress and to work with OMB on remedial actions to bring the agency's financial management systems into compliance.

We support the goals of Senator Brown's proposal, which make permanent the work of FASAB and add additional emphasis on implementing the accounting standards. We will be glad to work with the Committee as it considers this proposal.

Key to the FASAB approach was extensive consultation with users of financial statements early in their deliberations to ensure that the standards will result in statements that are relevant to both the budget allocation process as well as agencies' accountability for resources. Users were interested in getting answers to questions on such topics as:

—*Budgetary integrity:* What legal authority was provided to finance government activities and was it used correctly?
—*Operating performance:* How much do programs cost and how were they financed? What was achieved? What are the government's assets and are they well managed? What are its liabilities and how will they be paid for?
—*Stewardship:* Has the government's overall financial capacity to satisfy current and future needs and costs improved or deteriorated? What are its future commitments and are they being provided for? How will the government's programs affect the future growth potential of the economy?
—*Systems and control:* Does the government have sufficient controls over its programs so that it can detect and correct problems?

Standards and reports addressing these objectives are being phased in over time. Since the enactment of the CFO Act, OMB's guidance on the form and content of financial statements has stressed the use of narrative "Overview" sections preceding the basic financial statements as the best way for agencies to relate mission goals and program performance measures to financial resources. Each financial statement includes an Overview describing the agency, its mission, activities, accomplishments, and overall financial results and condition. The Overview also should discuss what, if anything, needs to be done to improve either program or financial performance, including an identification of programs or activities that may need significant future funding.

Agencies are beginning to produce reports that do this. For example, SSA's fiscal year 1994 financial statement Overview presented a number of performance measures dealing with the adequacy of the trust fund, service satisfaction, promptness in issuing earnings statements and processing claims, and the adequacy of employee training.

Linking the costs of achieving these performance levels is the next challenge. In this regard, FASAB's cost accounting standards—the first set of standards to account for costs of federal government programs—will require agencies to develop measures of the full costs of carrying out a mission or producing products or services. Thus, decisionmakers would have information on the costs of all resources used and the cost of support services provided by others to support activities or programs—and could compare these costs to various program performance.

GPRA Implementation

GPRA sets forth the major steps federal agencies need to take towards a results-oriented management approach. They are to (1) develop a strategic plan, (2) establish performance measures to monitor progress in meeting strategic goals, and (3) link performance information to resource requirements through the budget. GPRA requires up to five performance budgeting pilots for fiscal years 1998 and 1999.

OMB will report the results of these pilots in 2001 and recommend whether performance budgets should be legislatively required.

Cultural changes in federal agencies are beginning as agency pilots develop strategic plans and performance measures. OMB also has prompted progress by giving special emphasis in the fiscal year 1996 Circular A–11, *Preparation and Submission of Budget Estimates*, to increasing the use of information on program performance in budget justifications. Moreover, OMB Director Rivlin instructed her agency to use performance information in making budget recommendations. In preparation for the fiscal year 1997 budget cycle, OMB held performance reviews in May with agencies on performance measures and recently issued guidance on preparing and submitting strategic plans. Further progress in implementing GPRA will occur as performance measures become more widespread and agencies begin to use audited financial information in the budget process to validate and assess agency performance.

OMB is also making efforts to design new financial reports based on FASAB's recommended standards that contain performance measures and budget data to provide a much needed, additional perspective on the government's actual performance and its long-term financial prospects. While there are a myriad of legislatively mandated reporting requirements which could be presented in separate reports, I think that decisionmakers would find that a single report relating performance measures, costs, and the budget would be most useful. This reporting approach is consistent with the CFO Council's proposal for an Accountability Report, which OMB is pursuing.

The Government Management Reform Act of 1994 authorized OMB, upon proper notification to the Congress, to consolidate and simplify statutory financial management reports. The CFO Council has proposed two annual reports, a Planning and Budgeting Report and an Accountability Report. The two consolidated reports would be used to present a comprehensive picture of an agency's future plans and performance by addressing (1) how well the agency performed (accountability) and (2) the road map for its future actions (planning and budgeting).

The consolidation of current reports into the Accountability Report would eliminate the separate requirements under various separate laws—such as GPRA, the Federal Managers' Financial Integrity Act, the CFO Act, and the Prompt Payment Act. The Planning and Budget Report is intended to provide a comprehensive picture of an agency's program and resource utilization plans within its strategic vision. It is supposed to link resources requested with planned actions.

OMB is undertaking to have six agencies [10] produce, on a pilot basis, Accountability Reports providing a comprehensive picture of each agency's performance pursuant to its stated goals and objectives. We agree with the overall streamlined reporting concept and believe that, to be most useful, the Accountability Report must include an agency's financial statements and the related audit reports. The ultimate usefulness of the Accountability Report will hinge on its specific content and the reliability of information presented. In this regard, OMB and the CFO Council will be more fully defining the information to be included in the Accountability Reports during the pilot phase. We will work with OMB and agencies throughout the pilot program. The pilot concept has worked well in the past under the CFO Act and GPRA.

Performance, Costs, and the Budget

Of course, the ultimate goal of more reliable and relevant financial data is to promote more informed decision-making. This requires that financial data produced be understood and used by program managers and budget decisionmakers. The changes underway to financial reporting have been undertaken with a goal of making financial data more accessible to budget decisionmakers. The budget community's involvement in the FASAB standard-setting process and OMB's accountability proposal have contributed to this. The future challenge is to further integrate financial reports with the budget to enhance the quality and richness of the data considered in budget deliberations. As I will discuss below, improving the linkages between accounting and budgeting also call for considering certain changes in budgeting such as realigned account structures and the selective use of accrual concepts.

Perhaps the chief benefit of improving this linkage will be the increased reliability of the data on which we base our management and budgetary decisions. From an agency perspective, having audited information on the value of assets and liabilities, as well as the full costs of program outputs, will permit more informed judgments in strategic planning and program priority setting. Coupled with internal control as-

[10] The six pilot agencies are the Departments of the Treasury and Veterans Affairs; the General Services, Social Security, and National Aeronautics and Space Administrations; and the Nuclear Regulatory Commission.

sessments, such information will also enable agencies to better target areas requiring greater management attention or reform. For example, as I discussed earlier, the IRS financial audit revealed that the accounts receivable inventory was largely uncollectible—important information that permits IRS to better target its collection resources and permits more informed appropriations decisions on the level of resources necessary to collect these funds.

From a budgetary decision-making perspective, the new financial reports will improve the reliability of the budget numbers undergirding decisions. Budgeting is a forward-looking enterprise, but it can clearly benefit from better information on actual expenditures and revenue collection. Numbers from the budget will be included in basic financial statements and thus will be audited for the first time.

Having these numbers audited was one of the foremost desires of budget decisionmakers consulted in FASAB's user needs study and stems from their suspicion—well warranted I might add—that the unaudited numbers may not always be correct. For example, decisionmakers rely on data based on IRS systems on the amounts of revenue collected for each type of tax. However, as highlighted earlier, our audit revealed that the IRS's reported revenue of $1.3 trillion for fiscal year 1994 could not be verified or reconciled to accounting records maintained for individual taxpayers in the aggregate and amounts reported for various types of taxes collected could not be substantiated. This means that the amount credited to the Social Security Trust Fund is different than the amount of social security taxes actually collected.

Financial audit reports have also revealed important information on the actual costs of credit programs which can inform future budgetary decisions. Specifically, the fiscal year 1994 financial audit reports of the Farmers Home Administration, the Federal Housing Administration, the Federal Family Education Loan Program, and the Small Business Administration revealed that agencies' estimates of the subsidy costs of their credit programs reflected in the budget are not accurate. Based on these audits, budget decisionmakers know that they have reason to question the amount of future budget requests for these programs.

The new financial reports will also offer new perspectives and data on the full costs of program outputs and agency operations that is currently not reported in our cash-based budget. Information on full costs generated pursuant to the new FASAB standards would provide decisionmakers a more complete picture of actual past program costs and performance when they are considering the appropriate level of future funding. For example, the costs of providing Medicare are spread among at least three budget accounts—the Federal Hospital Insurance Trust Fund, the Federal Supplementary Medical Insurance Trust Fund, and the Program Management account. Financial reports would pull all relevant costs together.

The different account structures that are used for budget and financial reporting are a continuing obstacle to using these reports together and may prevent decisionmakers from fully benefiting from the information in financial statements. Unlike financial reporting, which is striving to apply the full cost concept when reporting costs, the budget account structure is not based on a single unifying theme or concept. As we reported recently, the current budget account structure evolved over time in response to specific needs.[11]

The budget contains over 1,300 accounts, with nearly 80 percent of the government's resources clustered in less than 5 percent of the accounts. Some accounts are organized by the type of spending (such as personnel compensation or equipment) while others are organized by programs. Accounts also vary in their coverage of cost, with some including both program and operating spending while others separate salaries and expenses from program subsidies. Or, a given account may include multiple programs and activities.

When budget account structures are not aligned with the structures used in financial reporting, additional analyses or crosswalks would be needed so that the financial data could be considered in making budget decisions. If the Congress and the executive branch reexamine the budget account structure, the question of trying to achieve a better congruence between budget accounts and the accounting system structure should be considered.

In addition to providing a new, full cost perspective for programs and activities, financial reporting has prompted improved ways of thinking about costs in the budget. For the most part, the budget uses the cash basis, which recognizes transactions when cash is paid or received. Financial reporting uses the accrual basis, which recognizes transactions when commitments are made, regardless of when the cash flows.

---

[11] *Budget Account Structure: A Descriptive Overview* (GAO/AIMD–95–179, September 1995).

Cash-based budgeting is generally the best measure to reflect the short-term economic impact of fiscal policy as well as the current borrowing needs of the federal government. And for many transactions, such as salaries, costs recorded on a cash basis do not differ appreciably from accrual.

However, for a select number of programs, cash-based budgeting does not adequately reflect the future costs of the government's commitments or provide appropriate signals on emerging problems. For these programs, accrual-based reporting may improve budgetary decision-making. The accrual approach records the full cost to the government of a decision—whether to be paid now or in the future. As a result, it prompts decisionmakers to recognize the cost consequences of commitments made today.

The credit arena is a good example of how financial reporting has informed budget decision-making. Beginning in fiscal year 1992, accrual budgeting principles were applied to loans and loan guarantee programs with the implementation of credit reform. Cash treatment of these programs sent misleading signals by recording costs only when cash flowed in and out of the federal Treasury. Under this approach, loan guarantees, for example, were recorded as having no costs in the year in which program commitments were authorized, regardless of future costs flowing from this commitment. By contrast, under credit reform, the budget reflects the present value of subsidy costs to be incurred over time up front at the time when commitments are made.

It may be appropriate to extend the use of accrual budgeting to other programs, such as federal insurance programs—an issue we are currently studying at the request of the Chairman, House Budget Committee. For example, the cash position of the nation's deposit insurance system proved to be a lagging indicator of the underlying troubles faced by thrifts in the 1980s. An accrual approach, should it prove workable, would offer better information on the financial condition of various federal insurance programs.

Putting It All Together

Mr. Chairman, thanks in large part to the legislative impetus of the CFO and GPRA Acts—efforts led by this Committee—decisionmakers will ultimately have available unprecedented, reliable information on both the financial condition of programs and operations as well as the performance and costs of these activities. While these initiatives carry great potential, they require continued support by the agencies and the Congress. Consequently, this Committee's continued leadership and oversight will be important to sustain these initiatives and ensure their ultimate success.

Generating new kinds of information, however valuable, can be a difficult, intensive process calling for new skills and redeployment of resources. This is a particularly challenging task in our current budgetary environment. Fiscal constraints may make it difficult for agencies to allocate sufficient resources to information gathering and analysis while facing cuts in basic services. However, such information is vital to the downsizing process itself and can help us sort out the kinds of services and operations that government should be engaged in.

Finding the most effective reporting and analytical approaches will require a great deal of collaboration and communication. Appropriations, budget, and authorizing committees need to be full partners in supporting the implementation of these initiatives. This Committee could be instrumental in fostering a constructive dialogue and gaining their support, which is vital to obtaining the resources and investment needed to carry out these efforts.

This type of partnership is needed to better link financial and performance data to the budget and program decision-making. The development of new information may for a time outpace the capacity of the process to fully utilize it. Just as federal accounting standards are being tailored to better address the unique needs of federal policymakers, the cost concepts used in budgeting, as well as the budget presentations themselves, may warrant reconsideration. This calls for a concerted congressional effort to rethink how the budget should be structured and presented to best take advantage of this new information. Again, the Committee could be instrumental in bringing together key congressional stakeholders to consider appropriate changes.

Finally, the Committee can continue to support evolutionary refinements to reporting approaches. For example, the new financial reports can be even more useful when they are streamlined, rather than the present approach of generating separate reports. I have been stressing an approach in which performance measures and costs are reported together and linked to budget data within a single report. This approach is consistent with the CFO Council's proposal for an Accountability Report, which we support.

IMPROVING SINGLE AUDIT LEGISLATION

Mr. Chairman, in addition to strengthening financial management at the federal level this committee is also considering legislation to improve the effectiveness of accountability for federal payments to the state and local levels through the single audit process. Single audits are important accountability tools over the hundreds of billions of dollars that the federal government provides to state and local governments and nonprofit organizations.

In June 1994, we reported [12] to the Committee on the Single Audit Act's important role. It has helped institutionalize fundamental elements of good financial management in state and local governments, such as preparing financial statements in accordance with generally accepted accounting principles, obtaining annual independent comprehensive audits, assessing internal controls and compliance with laws and regulations, monitoring subrecipients, tracking federal funds, and resolving audit findings.

In addition, the single audit process is an effective way of promoting accountability over federal assistance because it provides a structured approach to achieve audit coverage over the thousands of state and local governments and nonprofit organizations that receive federal financial assistance. Moreover, particularly in the case of block grants—where the federal financial role diminishes and management and outcomes of federal assistance programs depend heavily on the overall state or local government controls—the single audit process provides accountability by focusing the auditor on the controls affecting the integrated federal and state funding streams.

Mr. Chairman, let me emphasize that block grants need not mean the absence of federal accountability provisions. Our extensive studies of the block grant experience in the 1980s led us to conclude that reasonable financial and program accountability provisions can help sustain block grants as a stable source of intergovernmental aid. Of course the definition of what is reasonable can be controversial. Overly-intrusive accountability provisions can threaten to overturn the efficiencies gained from flexible funding, while overly-limited provisions can undermine continued congressional support for the programs by depriving the Congress of information on how the funds are used and what results are achieved.

Clearly, block grants call for a careful balancing of state and federal concerns. It is in this context that the Single Audit Act can play an especially helpful role in promoting financial accountability for the proper stewardship of federal funds. The act's focus on overall state controls applied to state entities supported with federal and state funding is very consistent with the block grant approach where states are encouraged to manage federal and state funds on an integrated basis to support state priorities. It also gives state officials an annual report card on the financial management of their own entities.

While strongly supporting the single audit concept, we have identified opportunities to strengthen the single audit process while at the same time reducing the burden on state and local governments and nonprofit organizations. The legislation this committee is considering to amend the Single Audit Act would strengthen the single audit process in several key areas.

First, the bill would expand the Single Audit Act to include nonprofit organizations. The act currently applies only to state and local governments while nonprofit entities are administratively covered under an OMB Circular. Expanding the Single Audit Act to include nonprofit organizations establishes uniform single audit requirements for state and local governments and nonprofit organizations, which would accomplish what this committee contemplated when the act was debated.

Second, the dollar threshold that establishes which nonfederal entities must have audits under the act would be raised. Raising the minimum threshold from $25,000 to $300,000 would exempt thousands of entities from federally mandated audits while still covering 95 percent of federal assistance to state and local governments.

Third, programs would be selected for testing based on risk. Currently, the act requires auditors to select and test programs based solely on the amount of federal financial assistance the programs receive. Adopting a risk-based approach would increase the effectiveness of the single audit process.

Fourth, the single audit reports would be more useful. Program managers we contacted did not find current reporting to be user friendly, principally because of the number of auditor's reports. Single audit reports often include seven separate reports from the auditor. The proposed legislation would require auditors to include a summary of the results of the work. OMB adopted this approach several years ago at the federal level by including in financial statement audit reports under the

[12] *Single Audit: Refinements Can Improve Usefulness* (GAO/AIMD–94–133, June 21, 1994).

CFO Act a new Overview section highlighting key results. We found that it was extremely helpful in providing insights to report users.

Fifth, reducing the reporting time frame from the currently allowed 13 months to 9 months would significantly improve the timeliness of the reports. Timeliness alone does not determine the value of a report. But, the lack of timeliness can seriously degrade the value of a report. We understand that some auditors have concerns about meeting a shorter time frame. However, we believe that oversight of the hundreds of billions of federal dollars covered by the single audit process is degraded by reports that are issued more than a year after the end of the period audited. Over time, I hope that it will be the rule, rather than the exception, for the audit reports to be submitted in less than 9 months.

Sixth, the legislative proposal would provide greater flexibility than the current act allows in carrying out this important oversight activity. The proposed legislation does so by providing the OMB Director authority to adjust some aspects of the single audit process to mesh with changing circumstances. For example, the OMB Director could authorize pilot projects to test alternative ways of achieving the goals of the legislation. The authorities provided the Director should not increase the burden on nonfederal entities. Rather, it is designed to make the Single Audit Act process adaptable to changing circumstances while continuing to promote sound financial management and provide effective oversight over federal resources.

The 10 years of experience under the Single Audit Act has shown that the single audit process is a highly effective way to provide accountability for federal awards to state and local governments. The proposed amendments would strengthen this important accountability tool and reduce the burden on thousands of entities. We fully support their enactment.

Mr. Chairman, this concludes my statement. I would be happy to now respond to any questions.

ATTACHMENT I

RECENT GAO TESTIMONY ON THE BENEFITS ON PREPARING AND AUDITING AGENCYWIDE FINANCIAL STATEMENTS

Financial Management: Momentum Must Be Sustained to Achieve the Reform Goals of the Chief Financial Officers Act (GAO/T–AIMD–95–204, July 25, 1995).

Financial Management: CFO Act Is Achieving Meaningful Progress (GAO/T–AIMD–94–149, June 21, 1994).

Improving Government: GAO's Views on H.R. 3400 Management Initiatives (GAO/T–AIMD/GGD–94–97, February 23, 1994).

Improving Government: Actions Needed to Sustain and Enhance Management Reforms (GAO/T–OCG–94–1, January 27, 1994).

PREPARED STATEMENT OF G. EDWARD DESEVE

Mr. Chairman, Members of the Committee, I am pleased to be here today to provide an overview of the state of financial management in the Federal Government. In my testimony, I will draw heavily from the July 1995 report entitled, "Federal Financial Management Status Report and Five-Year Plan." This annual report, required by the Chief Financial Officers (CFOs) Act, reflects an overview of the status of Federal financial management and plans for improvement. This report was jointly prepared by the Chief Financial Officers Council and the Office of Management and Budget (OMB).

First, let me thank this Committee for the work it has done to support the CFOs Act, improve Federal management, and restore the public's confidence and trust in Government. The CFOs Act is only one of several pieces of legislation that this Committee has sponsored, all of which build a firm foundation for better management of Federal resources. The CFOs Act and its subsequent modification by the Government Management Reform Act (GMRA) of 1994, the Government Performance and Results Act (GPRA) of 1993, as well as earlier legislation such as the Federal Managers' Financial Integrity Act and the Inspector General Act together establish a framework for improved accountability, and better information for decision-making by the Congress and the President. These Acts, taken as a whole, will lead to a Government that can provide accurate and timely information to its citizens and for its leaders, and permit decisionmaking based on sound information. These laws together provide us with the framework and the tools to improve the management of the Federal Government and to restore the public's trust in its government. Throughout my testimony, I will emphasize the ways in which these statutes work together and build upon each other to achieve our mutual goal of improved Federal accountability.

Also, I would like to draw special attention to the work of the Chief Financial Officers Council. The CFO Council is composed of all of the CFOs and Deputy CFOs in the 24 agencies subject to the CFOs Act, as well as officials from OMB and the Department of the Treasury. Since May 1994, this Council has taken a significant leadership role in setting government-wide priorities for financial management. The Financial Management Status Report and Five-Year Plan as noted above was jointly drafted by OMB and the CFO Council for the first time this past year. The CFO Council set priorities and developed objectives and work plans to achieve these priorities. The three top priorities set by the Council are: improving financial systems, implementing the Government Performance and Results Act, and issuing accounting standards and financial statements.

The Chairman has asked that I address the status of CFOs Act, GMRA, and GPRA implementation; the role of Congress in assisting in implementation of these statutes; OMB's proposal for consolidating certain financial reports into an Accountability Report; proposed amendments to the Single Audit Act; and Senator Brown's proposed "Accounting Standardization Act." My testimony will cover these matters and other priorities of OMB and the agency Chief Financial Officers.

Chief Financial Officers Act Implementation

Organization

The CFOs Act establishes a series of requirements for each of now 24 agencies. (Originally, the CFOs Act listed 23 agencies; with the establishment of the independent Social Security Administration (SSA) in March, 1995, there are now 24 agencies subject to the CFOs Act.) Along with establishing a Chief Financial Officer (Presidential appointment with Senate confirmation for 16 of the 24 agencies subject to the Act), and a career Deputy CFO in each of the 24 agencies, the Act requires that agencies develop integrated financial systems; have the ability to record financial transactions in a proper, accurate, and timely manner; and that certain pilot organizations and all commercial, trust and revolving accounts prepare and have audited financial statements. This latter requirement was expanded in the GMRA to require that all agencies subject to the CFOs Act prepare and have audited, organization-wide financial statements for fiscal year 1996 and that there be a government-wide financial statement prepared and audited for fiscal year 1997.

With respect to organization and personnel, there are well-qualified individuals holding CFO and Deputy CFO positions in all 24 agencies. The CFO Council published a paper, "The CFO's Role in Strengthening Financial Management" in 1994, and is currently reviewing OMB's 1993 guidance on CFO Qualifications and CFO Organizations. We expect that the Council will be proposing some minor modifications to these documents within the next few months. Discussions are on-going with a few agencies regarding changes to their CFO organization and as these are finalized, the OMB Director will, as required by the Act, review and approve any necessary changes.

Financial Systems

Agencies are working towards the goal of integrated financial systems, the CFO Council's number one priority. Over the past 2 years, from 1992 to 1994, we have seen the number of agency financial management systems in operation decrease by 62. The CFO Council Financial Systems Committee, in conjunction with OMB, has just published the Fiscal Year 1994 Financial Management Systems Status Report. The report's primary objective is to be a tool for sharing information about federal financial management systems among agency managers who must gauge progress against guidelines contained in OMB Circular A–127 and make system decisions for their agencies.

The Joint Financial Management Improvement Program (JFMIP), a joint venture between OMB, GAO, Treasury and OPM, has published a series of documents to help agencies improve financial systems. These include the "Framework for Federal Financial Management Systems," and most recently, in September 1995, a revision to the "Core Financial System Requirements."

During September and October of this year, OMB met with all 24 CFOs Act agencies to discuss their progress and plans for improving financial management systems. All of the meetings were productive with good dialogue and exchange of ideas between the agencies and OMB. These meetings have helped to frame the future themes which OMB will pursue in improving financial management. As a result of these meetings, we have current information on the status of agency systems efforts to meet CFOs Act requirements.

The importance of commitment to financial management from the highest executive levels came through clearly in the system meetings. Agencies with top executives who are personally promoting sound financial management are improving financial systems and financial management practices most successfully. Some agencies have set up councils or boards to provide coordination and support throughout the agency which have been very effective. Many have internal CFO Councils which include CFOs from the bureaus as well as the departmental CFO. Others have an Information Resources Management Board, including the CFO, Senior IRM Official, and program officials, which oversees information technology projects, including financial systems, and make investment priority decisions.

Some agencies have shifted their financial management systems development strategy from a "big bang" approach to a more modular, incremental approach, which is consistent with the approach taken recently in some of the procurement reform and information technology management reform efforts. CFO offices are also changing from an internal CFO organization focus to a more agency-wide customer focus. Strategic planning processes are being developed with a strong customer service orientation.

Many agencies are using the concepts of business process reengineering to improve the processes they are using in addition to implementing new systems, seeing this as critical to coping with the cost and personnel reductions required. Other agencies could do more of this. Several agencies said that standardizing data definitions and usage across the agency, particularly data for financial and administrative purposes, has been a critical success factor in financial system improvement projects.

Many agencies are embracing off-the-shelf software and cross-servicing to meet their financial management system needs. However, we also heard many concerns about the quality of software available and the support provided by the vendors. The CFO Council and OMB have a task force addressing this and other strategic issues.

Audited Financial Statements

Another critical requirement of the CFOs Act is that agencies prepare and audit financial statements for certain pilot organizations and for all commercial, trust and revolving accounts. Audited financial statements increase the accountability of Federal managers, and, by fostering improvements in the underlying systems that produce the financial data, ultimately provide timely and accurate information for decisionmaking. By mid–1995, almost 60 percent of the 100 entities preparing audited financial statements required by the CFOs Act had received unqualified opinions, comparing favorably to 1991, when only 35 percent of the 55 entities audited earned unqualified opinions.

We have seen a marked improvement in agency acceptance of the rigors of financial statement preparation and audit since passage of the CFOs Act. This has been, perhaps, the most difficult transition for Federal financial managers and auditors to make. With GAO's strong support, the Federal Government has moved from skepticism about the usefulness of financial statements to growing support for their contribution to improved financial data. Acknowledging the value of audited financial statements, the Congress expanded the requirement in the Government Management Reform Act in 1994.

Government Management Reform Act Implementation

In 1994, GMRA expanded the requirement for audited financial statements to all of the activities of the 24 CFOs Act agencies, essentially making the statements organization-wide. GMRA also requires that a government-wide financial statement be prepared and audited for fiscal year 1997. OMB, GAO and the Treasury Department are working with the agencies to assure that both of these requirements are met.

In a manner similar to the financial systems meetings discussed above, GAO, OMB and Treasury are in the midst of a series of meetings with each of the agency CFOs and Inspectors General (IGs) to discuss their plans for the preparation and audit of organization-wide financial statements, and to determine if there are any obstacles which may prevent them from meeting this requirement. GAO joins us in these meetings to emphasize our shared goal, as well as the interrelationship of the agency-wide statements and audits and the government-wide statement and audit.

The IGs play an important role in CFOs Act and GMRA implementation. The IGs noted their support for the CFOs Act in a recent survey conducted for the Association of Government Accountants by Coopers and Lybrand (C&L). Eighty-four percent of the IGs stated that the benefit of financial statements justify the implementation costs. All of the IGs indicated that internal controls had improved under the CFOs Act. Conducting financial statement audits has required some IGs to reprioritize their work, so this statement of "value-added" is an important finding by the C&L survey.

IGs are finding different ways to conduct the financial statement audits. Some are forming effective partnerships with Certified Public Accounting firms and GAO. As a result, the IGs are gaining valuable experience in auditing agency financial statements and are maximizing the use of scarce IG contract and audit resources. For example, in 1993 the Inspector General of the Department of the Treasury worked closely with GAO in the audit of the U.S. Customs Service. The experience gained allowed the Treasury IG to conduct the 1994 audit entirely with Treasury IG staff The Office of Inspector General of the Department of Energy provides another example of an effective partnership. Planning an audit of the financial statements of an organization as complex as the Department of Energy is a major undertaking. The IG of DOE has contracted with a Certified Public Accounting firm to assist them in planning the audit of DOE's financial statements and in conducting certain aspects of the audit.

In addition, IGs are increasing their capability to perform financial statement audits through participation with GAO, OMB, Treasury, and agency CFO staff in a series of task forces established to develop solutions to complex crosscutting accounting and auditing issues that are critical to the successful completion of the agency-wide and government-wide audits required by GMRA.

Federal Accounting Standards

Underlying both the CFOs Act and GMRA is the need for a comprehensive set of Federal accounting standards and principles. The Federal Accounting Standards Advisory Board (FASAB) was established on October 10, 1990, by Memorandum of Understanding among the three principal agency heads (the Secretary of the Treasury, the Director of the Office of Management and Budget, and the Comptroller General) concerned with overall financial management in the Federal Government. At that time, the Federal Government did not have a comprehensive set of accounting standards. However, it was recognized that a comprehensive set of accounting standards was needed, and that compliance with these standards must be measured on a regular basis in order to ensure the integrity of the financial information reported to the American taxpayers, managers, elected officials, and policy makers.

By early spring, FASAB will have recommended a comprehensive framework for Federal financial reporting and the basic standards needed to carry it out. To date, FASAB has completed work on the following basic concept statements, accounting standards, and cost standards and they have been adopted by the three principals (OMB, GAO and Treasury):

- "Objectives of Federal Financial Reporting"
- "Entity and Display"
- "Managerial Cost Accounting"
- "Accounting for Selected Assets and Liabilities"
- "Accounting for Direct Loans and Loan Guarantees"
- "Accounting for Inventory and Related Property"
- "Accounting for Property, Plant and Equipment"

The following standard has been recommended by FASAB, and is under consideration by the three principals:

- "Accounting for Liabilities"

Finally, the following two standards are substantially complete and FASAB expects to make its recommendations to the three principals by early spring:

- "Accounting for Revenue and Other Financing Sources"
- "Supplementary Stewardship Reporting"

Once issued by OMB, these standards become GAAP—Generally Accepted Accounting Principles—for Executive Branch agencies. After issuing the standards, OMB will fulfill its responsibility to prescribe the form and content of agency financial statements by modifying its existing "Form and Content of Financial Statements" guidance to incorporate the new standards. The revised "Form and Content" guidance is expected to be completed by late next summer.

With respect to Senator Brown's proposed legislation, "Accounting Standardization Act," we believe that the process for establishing accounting standards as envisioned by the agreement between GAO, OMB and Treasury is working, as reflected in the above status report. We share with Senator Brown the goal that all government entities account for similar activities consistently and in the same manner from one fiscal year to the next. We believe that the Memorandum of Understanding signed by GAO, OMB and Treasury, and the related financial statement preparation and auditing requirements of the CFOs Act and GMRA achieve for us the same end without further legislation. We would be happy to continue to have a dialogue with this committee and Senator Brown to further explore the ramifications of the Senator's proposed legislation.

GOVERNMENT PERFORMANCE AND RESULTS ACT IMPLEMENTATION

GPRA is intended to transform fundamentally how government programs and operations are managed. GPRA requires that: (i) Federal agencies prepare strategic plans, with an initial plan to be submitted to OMB and the Congress by September 30, 1997; (ii) Federal agencies prepare annual performance plans, setting out specific performance goals for a fiscal year, starting with fiscal year 1999; (iii) OMB prepare a government-wide performance plan based on agency plans with the level of program performance to be achieved corresponding to the finding level in the President's Budget, starting with the fiscal year 1999 budget; (iv) Federal agencies submit an annual report to the President and Congress which compares actual performance with the goals that were previously set in the performance plan, with the first report 6 months after the end of fiscal year 1999; and (v) the Act includes provisions giving managers greater flexibility by allowing the waiver of various administrative controls and limitations; in return managers are expected to be more accountable for the performance of their programs and operations.

We are in the mid-point of this 4 year period for changing government processes, systems, and practices before the law takes full effect in 1997. Recognizing the comprehensive nature of GPRA, the CFO Council made GPRA implementations its second highest priority.

In the CFO Council's May 1995 report, "Implementation of the Government Performance and Results Act," the Council stated that: "Existing planning, budgeting, program evaluation and fiscal accountability processes should be integrated with GPRA requirements to ensure consistency and reduce duplication of effort. In addition, other management improvement efforts, such as implementation of the CFO Act and FMFIA, customer service initiatives, reengineering, TQM, etc. should be incorporated into the GPRA framework to capitalize on the synergy and availability of key information and to improve responsiveness to customers and other stakeholders."

Prior to GPRA coming into full effect, the law provides for several sets of pilot projects to test and demonstrate whether performance plans and performance reports will work as intended. Activities in 27 departments and agencies have been designated as performance measurement pilots, with over 70 individual pilot projects. The pilot projects range from the very large—the entirety of the Social Security Administration and the Internal Revenue Service—to the very small. Nearly 450,000 civilian and military employees are covered by these pilot projects. Depending on when they were designated, the pilot projects have submitted up to three separate annual performance plans. With the final set of plans submitted in the Spring of 1995, assessments are now being done on both the agency experience and the overall quality of these plans.

Anticipating the requirement for strategic plans, OMB issued two important documents in September 1995—a memorandum from Director Alice Rivlin to agency heads entitled, "Strategic Plans, Budget Formulation and Execution" and a new Part 2 to OMB Circular A–11 (Preparation and Submission of Annual Budget Estimates) providing instructions on the preparation and submission of agency strategic plans. In the memorandum, the Director stated that the OMB A–11 revision is "the first step in a larger effort to link various GPRA requirements to the budget process."

To better prepare for GPRA implementation, OMB conducted Spring Performance Reviews in 1995 of all departments and major agencies. These reviews examined the availability, current and prospective, of performance information for use in the fiscal year 1997 and future-year budgets.

OMB is also in the midst of an effort to demonstrate the feasibility of consolidating various planning and reporting requirements, and more closely integrating these with budget formulation and execution. The objective of this work is to connect resources to results so that the Government will be able to answer the question: "What are we getting for what we are spending?"

Accountability Reports

The CFO Council, in a January 1995 report entitled "Streamlining Government-wide Statutory Reports" proposed that there be two annual reports—a Planning and Budget Report and an Accountability Report. The Planning and Budget Report, consistent with OMB's revision of Circular A–11, addresses the integration of GPRA with other current requirements. The Accountability Report proposes to consolidate information obtained under the FMFIA and CFOs Act, and other statutes into a single Report. As agencies implement GPRA, performance information will be included in the Accountability Report.

The rationale for these consolidated reports is that they will present a comprehensive picture of agency performance, will report essential and relevant information, will link program performance with how well an agency is managed, and provide some flexibility in reporting format. These reports will provide Congress and the public with comprehensive, clear and concise financial and performance information.

GMRA section 404 permits the Director of OMB to consolidate or adjust the frequency and due dates of any statutorily required report for which OMB has financial management responsibility between January 1, 1995 and September 30, 1997, after consultation with the Congress. Under this authority, OMB has proposed to the Congress that we pilot test an Accountability Report in six agencies (Treasury, Veterans Affairs, General Services Administration, National Aeronautics and Space Administration, Nuclear Regulatory Commission, and Social Security Administration). The Accountability Report would consolidate the FMFIA report, the audited financial statement, and GPRA information, as available, into a single document to provide the Congress and the President with information in one place on how well an agency is managed and how well it is performing its mission.

FMFIA requires that an agency report in December of each year on the status of its internal controls, and identify any material weaknesses and the schedule for correcting these weaknesses. The CFOs Act requires that the audited financial statement include a report by the auditor on agency compliance with law and regulation, and an auditor's report on internal controls. The CFOs Act also requires that agency financial statements include program performance information. An agency Accountability Report would consolidate these very similar requirements into a single Accountability Report.

The CFO Council also proposed that agencies include performance information in their Accountability Report in advance of GPRA deadlines, and that certain other financial reporting, such as that required by the Prompt Payment Act, be included in the Accountability Report.

There is already good reason to believe that an Accountability Report is possible. The Social Security Administration, in its fiscal year 1994 Financial Statement, opens with an agency overview, and then states the SSA Mission, followed by ten pages of Key Goals and Performance Measures. The financial statements themselves follow, with supplemental information, and the auditor's report completes the package. With some modification, this SSA Financial Statement can become the agency's Accountability Report, including FMFIA assurances and identification of material weaknesses. Since SSA plans to produce this consolidated report in December 1995 covering its fiscal year 1995 activities, it will meet all the submission dates for the associated statutes, thus meeting all mandated deadlines. Of the other agencies in the Accountability pilot, only GSA expects to report by December.

The remaining four agencies that have volunteered to pilot test an Accountability Report for fiscal year 1995, will not be able to meet the earliest statutory deadline (December). Therefore, we need the Congress' acknowledgment that the Accountability Report pilot is a worthwhile demonstration project.

The concept of an Accountability Report is, we believe, consistent with Senator Roth and Senator Glenn's December 8, 1994 letter to Comptroller General Bowsher that a "practical management framework" is needed to coordinate the management reforms that have been enacted over the past 15 years.

Debt Collection Improvement Act of 1995

Finally, I would like to discuss two important items on our legislative agenda. The first, the Debt Collection Improvement Act of 1995 (H.R. 2234 and S. 1234) has strong bipartisan support. The CFO Act charges agency Chief Financial Officers with implementing agency asset management systems for credit management and debt collection (Section 902). The CFO Council has been extremely active in the development of the Debt Collection Improvement Act of 1995 (H.R. 2234 and S. 1234). This bill presents an opportunity for the Congress and the Administration to create a new Government-wide debt management program. As we reported in the "Federal Financial Management Status Report and Five-Year Plan," the current trends in delinquencies indicate that we need to improve debt collection through the use of modern techniques, enhanced systems and well-trained staff. Once the proposed Debt Collection Act of 1995 is enacted, it gives CFOs and program managers the tools and the incentives to take a fair and consistent, businesslike approach to debt collection. This bill can save billions ($2 billion over 5 years) by improving the annual collection of delinquent debt, preventing delinquencies, and lowering the deficit. This bill has strong bipartisan support, and OMB and the CFO Council look forward to working with you on its passage.

SINGLE AUDIT ACT

The other legislative item I would like to mention is the Single Audit Act (SAA) of 1984. One of the primary objectives of the SAA was to improve financial management of State and local governments that administer Federal awards. Studies show that the single audit process is working well to achieve its intended objective. However, our experience and these same studies indicate that improvements are needed to make this process more effective and cost-beneficial. Future amendments to the Act should provide legislative and regulatory relief to recipients of Federal awards (i.e., cut some of the red tape attached to Federal awards) while maintaining an appropriate level of accountability over these awards.

OMB is working closely with many organizations directly affected by single audits including GAO, Federal funding agencies (program managers and IGs), State governments (program managers and State auditors), other Federal award recipients, and public accounting professionals to develop proposals to improve the single audit process.

One of the most significant recommendations for improvement to the Act is the proposal to increase the threshold amount which triggers a single audit requirement from $25,000 to $300,000 in Federal awards per year. It is estimated that with the current threshold of $25,000, over 99 percent of Federal awards to governments are covered under single audits. If the threshold were raised to $300,000, it is estimated that over 95 percent of Federal awards would continue to be covered, yet thousands of recipients would no longer have a single audit requirement because they receive less than $300,000 in Federal awards. There is widespread support among organizations affected by single audits for increasing the threshold. OMB believes this increase would provide substantial relief to recipients without increasing the Federal Government's risk.

Another issue under consideration would involve a risk-based approach to determining major programs—that is, those programs that get most audit attention or focus during a single audit. Currently, major programs are determined using a formula which results in the largest programs administered by a recipient being audited as major programs year after year, regardless of whether problems were identified. Under a risk-based approach, OMB would prescribe criteria for risk, in addition to the monetary value of the program, which should be considered when determining which programs to audit as major. The advantage of a risk-based approach is that it would be designed to better align audit resources with audit risk.

Several other issues under consideration involve providing greater flexibility in implementing the Act. Experience has shown that some flexibility is needed to improve the single audit process in the future as conditions, risks, and the grant administration function evolve. This is particularly evident with respect to the audit threshold of $25,000 described above, which was established in the Act. As a result, changing the current threshold requires a statutory amendment. Flexibility would be increased by having the Act call for a biennial assessment of the adequacy of the threshold and authorize OMB to increase the threshold further in future years, as considered necessary. Such a provision would add greater flexibility to the Act and would permit more timely increases in the threshold, as warranted.

It has also been suggested that the Single Audit Act could have a significant impact on the ability of certain Federal agencies (particularly those agencies in which a large portion of their activities and services are delivered through Federal awards) to comply with the requirements of the Government Management Reform Act of 1994 and the Government Performance and Results Act of 1993. Increased flexibility provided in SAA could allow for using the single audit mechanism in the fixture to provide information about how well Federal programs are meeting their intended missions, goals, and objectives and may provide information to be included in agency-wide and government-wide financial statements.

This concludes my remarks. I will be happy to respond to any questions.

PREPARED STATEMENT OF WILLIAM R. PHILLIPS

Thank you Mr. Chairman and members of the Committee, for the opportunity to represent Coopers & Lybrand in today's hearing. I am William Phillips, a partner of Coopers & Lybrand Consulting, in our Government Consulting Practice, a group of over 500 management, finance, and information technology consultants headquartered in the metropolitan Washington, D.C. area. Many of our clients are federal agencies. Our work includes assisting them to implement the requirements of the Chief Financial Officers Act of 1990 (CFO Act) and other associated legislation such as the Government Performance and Results Act of 1993 (GPRA) and the Government Management and Reform Act of 1994 (GMRA), the subjects for today's hearings.

My testimony presents the results of a survey of federal agencies about progress and issues with the CFO Act and related legislation. The results show strong support for and progress in implementing the Act. The Committee and Congress should be proud of helping to make this legislation a force for fiscal and program effectiveness. However, the survey reveals some issues that Congress must address in order to ensure continued progress.

Background

During the summer of 1995, the Association of Government Accountants and Coopers & Lybrand L.L.P. surveyed nearly 100 Federal agencies to assess the status of their implementation of the Chief Financial Officers (CFO) Act of 1990 and other companion legislation. Surveys were sent to senior financial managers, inspectors general (IG) and selected program managers at each of the agencies charged with implementing the Act.

The results of this survey illuminate key concerns agency personnel share as they work to implement the Act in their agencies. The survey employs some common questions for financial managers, inspectors general and program managers, and these common questions reveal how the groups concur on some issues and differ on others. Combined, the results of the survey confirm the value of the CFO Act and provide insights into the challenges facing the Federal financial community as the March 1, 1997, implementation deadline approaches.

This was a mailed survey. The chart below displays the response rates for each part of the survey.

	Agencies			People		
	# of Agencies Sent Surveys	**# of Agencies Returned Surveys**	**Response Rates**	**# of People Sent Surveys**	**# of People Returned Surveys**	**Response Rates**
Financial Managers	94	71	76%	250	124	50%
Inspectors General	33	26	79%	33	26	79%
Program Managers	94	52	55%	470	150	32%

CFO ACT SURVEY RESPONSE RATES

Survey Findings

Leadership. The majority of senior financial managers (75%), inspectors general (81%), and program managers (66%) noted broad leadership support for implementing the CFO Act. Very few of the financial managers or IGs felt that leadership was a problem.

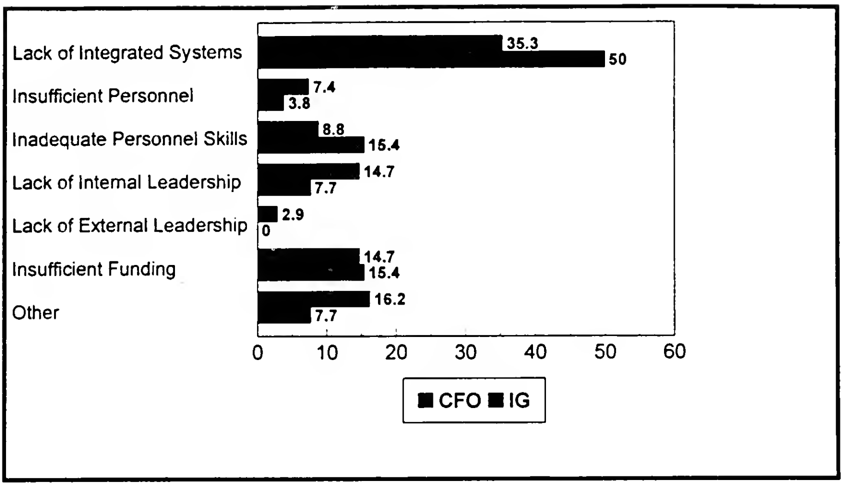
Benefits of the CFO Act. All three groups (70 percent, 85 percent and 61 percent respectively) agree that the benefits of annual financial statements justify the initial costs and efforts toward that end. Almost all the inspectors general report that the CFO Act has contributed to improved financial systems (88%); improved financial data (96%); and improved internal control procedures (100%). Financial managers and inspectors general agreed that the process of developing the statements is more valuable than the actual statements themselves. By this, they mean the process of working toward a full understanding of what government costs are, and what drives those costs.

Progress toward Implementing the CFO Act and the GPRA. To gauge each agency's progress toward implementation, we reviewed the responses from the most senior financial manager at each of the 71 participating agencies and the responses from the 26 Offices of the Inspector General. Regarding progress toward some of the reporting requirements of this legislation, the majority of financial managers (70–80%) reported that they currently prepare most of the reports and documents required by the CFO Act and GPRA. Although much work remains in the area of performance measures, most agencies (86%) reported at least partial progress. Progress was reported on integrating financial statement information into the budget process by nearly half of the respondents; however, about one third (34%) did not feel that they were making progress toward that end.

(Numbers in Percent)	Yes	No	Partial	Do Not Know	Total %
A Strategic Plan	78.9	7.00	12.70	1.4	100
Statement of Financial Position	83.1	4.20	8.50	4.2	100
Statement of Operations (and Changes In Net Position)	74.6	7.00	11.30	7	100
Statement of Cash Flows	71.8	15.50	7.00	5.6	100
Statement of Budgetary Resources & Actual Expenses	80	10.00	7.10	2.9	100
Performance Measures	54.9	9.90	32.40	2.8	100
Financial Program Performance Measures	42.3	14.10	39.40	4.2	100
Executive Info System (EIS) types of reports	48.6	17.10	28.60	5.7	100

Financial Manager's Response to the Question: Which of the Following Does Your Organization Currently Prepare?

Challenges. To gauge each agency's progress toward implementation, we reviewed the responses from the most senior financial manager at each of the 71 participating agencies and the responses from the 26 Offices of the Inspector General. Both the senior financial managers and the inspectors general understand that there are a variety of challenges facing organizations responsible for implementing the CFO Act. The lack of integrated systems received the most votes from both communities (35.3 percent and 50 percent respectively) as the greatest barrier to their organizations' ability to implement the CFO Act. Insufficient funding received the second largest number of votes as the greatest barrier by both groups (14.7 percent and 15.4 percent respectively). However, tied with insufficient funding for the senior financial managers was the lack of internal leadership, while IGs gave equal votes to inadequate personnel skills. The chart below shows the findings from both groups surveyed.



Response (In Percent) to the Question: What is the Greatest Barrier to Your Organization's Ability to Implement the CFO Act?

In addition to barriers in implementing the CFO Act, about one third of the IGs (32%) identified a lack of supporting documentation as the greatest barrier to accomplishing an effective audit of their organization's CFO Act financial statements. This finding is consistent with the finding that a lack of integrated systems is the greatest barrier to CFO Act Implementation. Clearly, if the accounting systems are not integrated with the functional systems, an organization is hard pressed to develop accurate financial statements and the auditors are unable to render an opinion because of the paucity of back-up data needed from functional managers.

Employees who are reluctant to change in response to new requirements of the CFO Act and other new legislation was not viewed by most financial managers (66%) as a significant problem. However, nearly half (47%) of the program managers thought this was a problem in their own offices.

Budget Cuts. The financial managers and IGs were clear that downsizing and budget cuts are affecting their operation. Only one out of four financial managers (76%) reported that his or her office has received more money for taking on the responsibilities of the CFO Act. However, a majority of the financial managers (64%) and IGs (58%) say downsizing is hampering their implementation of the CFO Act, and about the same percentages reported that the National Performance Review's emphasis on streamlining administrative functions was doing the same.

Concluding Notes

In summary, Mr. Chairman, this survey shows there has been much progress by most agencies over the past 5 years. Moreover, there appears to be wide acceptance of the CFO Act within financial and audit communities, as well as with the program managers.

In closing, I would like to offer two recommendations to facilitate continued implementation of the CFO Act. First, let's think about what is going to happen to all this new financial information. The first 5 years of the CFO Act have been a situation where the Congress demanded certain financial and program information from the agencies, sending them scrambling to collect, analyze, and report that data. Much good has come of that effort, as witnessed by our survey respondents, the Comptroller General, and others. But that is not enough to sustain the effort. This year and in the years that follow, Congress must use an agency's financial statements when deliberating that organization's budget requests. This would visibly integrate the intent of the Act into the budget process. If the Congress demands

Second, implementing any new program requires resources, and Congress should avoid summarily cutting funding related to the CFO Act. In this same vein, we believe that the Office of the CFO and the Office of the Inspector General should be protected from excessive downsizing cuts. Clearly, investing a few million now to fully implement the CFO Act can yield billions of dollars in savings and cost avoidance in the future.

Congress should capitalize on the progress to date with implementing CFO Act requirements by encouraging agencies to share best practices and innovative approaches to tough issues. Also, agencies that have made significant improvements should be recognized for their achievements. Supporting the CFO Act is smart business and we applaud this Committee's efforts toward that end. Mr. Chairman and members of the Committee, thank you for the opportunity to appear before you today.

Mr. Phillips can be reached at Coopers & Lybrand L.L.P., 1751 Pinnacle Drive, McLean, VA 22102–3811, phone 703–918–3630, fax 703–918–3764. Coopers & Lybrand will be pleased to provide more information on the survey; please contact Mr. Andrew West at the address or fax above, or by calling him at 703–918–3614.

PREPARED STATEMENT OF KURT R. SJOBERG

Good morning, Mr. Chairman and members of the Committee. I am Kurt Sjoberg, the State Auditor of California.

It is a pleasure to speak to you this morning on federal financial management, especially as it relates to the Single Audit Act of 1984, and the proposed legislation to amend it. I am currently chairman of the National State Auditors Association's Single Audit Committee, and in my capacity as California's State Auditor, my office is responsible for performing the largest Single Audit in the nation. As such, I will wear two hats today and share the views of State Auditors in general, and my own as the independent auditor of a large State.

First, let me say that the Single Audit Act is an important cornerstone in the state/federal partnership over the financial accountability and oversight of federal grant and program funds. My state audit colleagues and I believe that the act has been a success and has fully met the objectives it was intended to achieve. We also believe, however, that after 10 years there are improvements to the act that are needed to address changes in the auditing profession and in federal, State and local government financial management. We would also like to commend the Committee's staff, the Office of Management and Budget and the General Accounting Office for their willingness to obtain the views the National State Auditors Association, its members and other professional groups on how the act should be amended. This open and constructive dialog goes a long way towards ensuring positive federal/state relations.

Federal / State Audits Prior to the Single Audit Act of 1984

Prior to the implementation of the Single Audit Act and OMB's Circular A–102, Attachment P, audits by the State and federal government were uncoordinated and often ill-timed. It was not uncommon for a subrecipient agency to have several federal and State auditors reviewing their activities at the same time. Not only was this burdensome, but often the auditors would examine the same records to test compliance with regulations or appropriateness of expenditures. Further, since each auditor had their own "unique" interests (e.g., a federal grant or a State contract) and due to limits on accessing the workpapers of another auditor, we did not rely on the work of others. Federal and State audit resources and dollars were certainly not being maximized. Due to this situation, federal, State and local government auditors and program officials joined forces in sponsoring and supporting the Single Audit Act of 1984 to alleviate this unneeded duplication and maximize the use of limited audit resources—whether at the federal, State or local levels.

Initial Implementation of the Act was Difficult

The Single Audit Act was premised on the concept that the recipient government would obtain a financial and compliance audit from a CPA or independent government auditor and the federal government would rely on this work. If the federal program agency or inspector general believed more in-depth auditing was needed on one of their programs, they would "build upon" the Single Audit, and thus, not duplicate audit work already performed.

While this idea was embraced by the federal community as the bill was being deliberated, after it passed, there were disagreements that caused some implementation problems. These disagreements centered around the federal Inspector Generals expecting that State auditors would do more audit work for them, and that they, in some way, could direct or mandate the work to be done. As one of the first States to embark on a statewide Single Audit, California was at the forefront of the negotiations that ensued with the Inspector Generals and OMB. Ultimately, because the act was well drafted, the state-federal audit partnership was resolved to the satisfaction of all State auditors.

After Ten Years There is a Need for Change

The Single Audit Act of 1984 has served us well, but over the past decade changes in the auditing profession, and in State and federal financial management, dictate that the act be amended. While there are several good reasons to amend the act, the following two are particularly noteworthy:

- *Current thresholds are too low:* Under the proposed amendments to the Act, many smaller local governments will be relieved of unreasonable audit mandates. The proposed minimum threshold to perform a single audit would be increased from $100,000 to $300,000 in federal receipts. This will generate savings to these local governments in reduced audit costs. Similarly, raising the maximum for large entities like California from the current $20 million to $30 million will reduce audit costs in larger States while only minimally reducing audit coverage of federal program expenditures.
- *Allow a risk-based audit approach:* Allowing the federal government and State and local auditors the discretion to focus audit resources where the potential for return is greatest makes good economic sense. Rather than being mandated to audit a particular grant year after year even when the potential for loss is low, using a risk-based approach allows the auditor to concentrate on programs that have been identified as "high-risk." This will certainly generate more corrective action and recoveries with the same audit investment.

Draft Legislation Addresses Most of the State Auditors' Concerns

As I mentioned at the outset, my colleagues and I have had several opportunities to provide input on the proposed legislation and find that almost all of our concerns have been addressed. We also believe that the draft legislation does not overly burden State auditors nor does it confer unreasonable powers with the OMB or other federal agencies. The National State Auditors Association has not had an opportunity to meet as a full group since the most recent draft legislation was presented to us. However, based on conversations I have had with a number of my colleagues, I am confident that NSAA will fully support the proposed legislation with only a few suggestions to improve or clarify the bill. These improvements relate to the definition of internal controls, clarification on the application of the 50 percent rule, and making copies of workpapers for the federal government. I have shared these issues with OMB and GAO staff, and the State auditors stand ready to assist in any way we can help to finalize the bill and facilitate its passage.

Thank you, that concludes my statement. I will be happy to answer any questions the Committee may have.

PREPARED STATEMENT OF TED SHERIDAN

Good morning. My name is Ted Sheridan. I am President of Sheridan Management Corp. and Chairman of the Financial Executive Institute's Committee on Government Liaison. Financial Executives Institute (FEI) is a professional association of 14,000 chief financial officers, treasurers and controllers from some 8,000 companies throughout the United States and Canada. The Committee on Government Liaison (CGL) formulates positions on economic and regulatory issues of concern to American business and offers private sector perspective and advice as a resource to those concerned with improvement of financial management of the U.S. Government.

It is a great privilege to present the views of CGL before the Committee on Governmental Affairs of the U.S. Senate shortly after the fifth anniversary of the signing of the Chief Financial Offers Act of 1990 (CFO Act or the Act). My association with the Act began well over a decade ago when, as CFO of a major industrial corporation, AMF, I began working with private and public sector organizations on a Grace Commission recommendation to create a Chief Financial Officer of the United States. This included testimony before the (then) House Government Operations Committee and twice before this Committee chaired by Senators Roth and Glenn respectively. At this juncture, it is appropriate to reflect on how far the CFO Act has advanced federal financial management improvement and what mid-course corrections are indicated to achieve the Act's intended purposes by the millennium in the year 2000.

A Scorecard of Progress

Impressive ground has been covered. The tentative pilot undertaking of the 1990 Act was buttressed by the Government Management Reform Act definitively extending CFO Act coverage to the 24 most important federal entities. This was further strengthened by the Government Performance and Results Act (GPRA) which dictates strategic planning, stated objectives and the means by which to measure progress towards those goals. Thus, we now have the legislative framework to mandate improved financial management.

The Financial Accounting Standards Advisory Board (FASAB) has come a long way in creating the conceptual structure required to permit application of Generally Accepted Accounting Principles to the specific and often conflicting conditions surrounding federal financial activity. FASAB has done highly creative thinking to establish innovative standards for complicated issues such as stewardship accounting for weapons systems and the ownership of trusts, public lands and monuments. FASAB has almost completed its work and we now have in place the standards required to audit federal government financial statements.

Similarly, the Office of Management and Budget (OMB) has taken a leadership role in the promulgation of guidance for compliance with the provision of a host of Acts and Regulations. Deputy Director John Koskinen and Comptroller Ed DeSeve have provided direction to the Chief Financial Officers Council formed under provision of the Act to address common interests of the CFOs. The composition of that Council is testimony to the quality of financial managers now holding these important posts. I am also pleased to mention the work of the U.S. Postal Service CFO, Mike Riley, a member of my FEI committee, who was recently cited in the prestigious CFO Magazine for his innovative *Economic Value Added* work there.

It is worth pointing out that many of these CFO's, and the Inspectors General and program managers of their organizations were interviewed for a survey recently released by the Association of Government Accountants and Coopers & Lybrand. A partner of Coopers & Lybrand, Mr. Bill Phillips, is here today on this panel. The survey shows overwhelmingly that these individuals support the Act and attest to its value in the improvement of management in the organizations. I think that the results of the survey represent a high tribute to the wisdom and foresight of this Committee and all who have supported the CFO Act.

The General Accounting Office (GAO) has exerted an extraordinary effort in fact-finding and analysis of systems and procedures needed to support compliance with the CFO Act and companion legislation. They have also provided advice and counsel to concerned departments and have reported on progress towards financial management improvement to the Congress. In particular, I would like to commend this Committee (and the House Committee on Government Reform and Oversight) for the leadership shown in maintaining momentum in pursuit of the goals of the Act.

Thus, with the outstanding work of these organizations, a firm foundation has been established to support the financial management improvements envisioned by the 1990 Act. Beyond that, we sense the resolve of department and agency leaderships for major advances. With this has come a heightened concern by the Congress and a spirit of cooperation by those charged with measuring the progress of the effort.

A Milestone Hearing

A particularly noteworthy event in this regard was a hearing this spring of the Subcommittee on Readiness of the Senate Committee on Armed Services where Comptroller General Chuck Bowsher commented favorably on Defense Secretary Perry's blueprint for achieving substantive improvement in financial management. He also suggested a four point program for the Department of Defense (DOD) to achieve the Secretary's objective. FEI shares his view on what must be done to go forward and that what remains to be accomplished is daunting. Nevertheless, we should not lose sight of the fact that much has been done to identify problems and to prepare the groundwork for moving forward to master these formidable obstacles.

At that same hearing, the CFO of DOD, Undersecretary John Hamre, provided a frank assessment of the myriad, unharmonized financial systems currently in place and the difficulties involved in providing appropriate financial management support. He also set forth steps already taken to shrink and streamline DOD's Defense Finance and Accounting Service (DFAS) and the reduction in size and complexity of DOD's once massive set of rules and regulations. Less tangible, but equally important as these measures was the evident sincerity of DOD's CFO in pursuit of financial management improvement and the shared support of the component service organizations. Also highly significant was the fact that this important military oversight committee expressed its concern for consistent progress towards improved financial management and offered its unqualified assistance. FEI believes this was a milestone hearing that witnessed a cooperative commitment to meet an unprecedented challenge in financial management.

FEI's Experience

FEI can attest to the involvement of the federal CFO community in efforts to advance financial management goals through its periodic meetings with individual CFO's as well as directly supporting the objectives of the CFO Council. In addition, FEI was approached by Air Force Assistant Secretary for Financial Management, Bob Hale, for assistance in complying with requirements arising from audits of their financial statements. This has led to active participation with his staff to study reporting for contingent liabilities and the development of guidelines for operations efficiency measurement. This work enabled us to reconfigure a program already in use by Air Combat Command to measure the potential financial obligations from environmental conditions at U.S. Air Force bases. As a consequence, the Air Force will adapt this study to comply with an important contingent liability issue confronting the service. In FEI's view, this approach could be used as a model for the other services and any other entity with similar problems. This work has given FEI a good look at the level of effort undertaken by the Air Force and the strides they have made. We are highly impressed at the support for the undertaking from the highest levels and the dedication of the financial management teams.

These observations about the ongoing financial management programs across the government hopefully reflect the appreciation FEI has for the progress made as a result of the enactment of the CFO Act. Nevertheless, at this juncture, it is important to have a clear view of what the desired condition should be in the year 2000 and what it will take to get there. Much has been written and said about the problems that continue to exist and how difficult the road to financial management improvement will be. As there are those much more qualified to comment on these matters, FEI will not presume to add to the list despite the concern we share. We feel it more appropriate to offer some perspective from private sector experience and a few concrete proposals for consideration. These will relate to the second and third Purposes set forth in the Act, the first being organizational and largely accomplished. These latter two relate to the systems and procedures required for the "production of complete, reliable, timely and consistent financial information for use by the executive branch of the Government and the Congress in the financing, management, and evaluation of federal programs"—"and to deter fraud, waste and abuse of Government resources."

Annual Reports

First, let us examine our recommendations on improvement in the usage of reports required by the Act. We believe Annual Reports with audited financial statements should be prepared that include a clear statement of the mission and objectives of the organization, the plan to achieve them and the financial resources required to support the undertaking. The Annual Report would, in effect, be the combined end product of both the CFO Act and GPRA. We believe that Annual Reports, as in the case of private sector corporations, should be the most important first impression given to the outside community and a lasting record of progress towards efficient, cost effective performance of stated mission objectives. These reports and accompanying audit findings and comments should be provided to concerned oversight and appropriations committees of the Congress as well as the House Committee on Government Reform and Oversight and this Committee of the Senate. This would provide these committees with critical insight as to the stewardship of the organizations under their purview. Hopefully, the Committees would, in the course of hearings and deliberations, examine critically the history of financial management before proceeding with the authorization and appropriation process during the budgetary cycle. This would forge the critical linkage among strategic planning, budgeting and financial reporting of actual results. This would also provide a function widely adopted in the private sector of financial and audit reports reviewed by corporate Boards of Directors on behalf of stockholders. In the case of the proposed review by Congress, it would be representing America's taxpayers.

Further, we would recommend that, until an entity has received an unqualified opinion on its financial statements, it accompany its Annual Report with 5 year Strategic and current year Tactical Financial Management Plans, indicating specifically the steps being undertaken to achieve a clean report. Beyond that, we would urge that a firm time limit of no more than 5 years be established for the achievement of an unqualified opinion. Lastly, we feel that sufficient resources in terms of qualified personnel and the funding of systems and procedures improvements must be provided to accelerate the pace of progress. In a slight twist of the old saying, "It takes money to save money." With a mere 5 percent reduction through savings and efficiency in federal outlays and assets employed, much of the agonizing policy decisions involved in balancing the budget could be eliminated because the government would be operated at a surplus with the current level of activity and investment or, alternatively, the federal debt could be reduced.

Steps to Achieve Clean Audits

First, break down massive, complex organizations into smaller, discrete, functional entities that individually work to achieve unqualified audits. This is permitted and encouraged by the FASAB guidance on Entities. This would allow departments and agencies to plan a program that shows progress, entity by entity, towards the ultimate goal of a consolidated statement receiving a clean opinion. This process has already begun in organizations such as the Department of Housing and Urban Development. To hold off examination of a major department such as DOD until auditability of all components has been achieved means that a decade or more will pass before even an attempt can be made for audited statements of the entire U.S. Government—an unacceptable state of affairs. By auditing functional entities on a prescribed, prioritized schedule, it will be possible to record systematic progress towards the goal of audited consolidated statements.

In the institution of a progressive program, two elements are important in determining priorities, timetables and allocation of resources. These are the significance of the entity to the basic mission of the organization and the current level of compliance with auditing standards. Thus, a functional organization on the leading edge of essential service delivery that possessed satisfactory financial management attributes would be designated an early candidate to pursue an unqualified opinion. Those entities, mission critical but lacking required financial systems and procedures, would receive focused attention and adequate resources to bring them into compliance at an early date.

Many entities supporting mission important functions such as procurement agencies and financial asset pools are currently unauditable—principally because the original cost of assets was never established or the value of contingent or intangible liabilities is difficult to ascertain. If entity systems and procedures are adequate to track future asset and liability values, then it is suggested that a Board of Valuation be appointed to establish entry point values using prescribed guidelines and their collective best judgement. Assets remote from the delivery of essential services and of questionable or unknown value could be segregated into fully reserved, off balance sheet accounts so as not to contaminate the financial statements of main line activities until valuation can be determined. Clearly, the Congress and the general public would like to know that an Air Combat Command fighter wing has its financial house in order rather than endure debate over the value of ancient ammunition stored in a desert depot.

A root cause of difficulty in providing clean audits is the lack of standard, double entry, transition-driven general ledgers, the heart of an accounting system. This is exacerbated by the lack of data entry integrity and the multiplicity of non-integrated feeder systems, not specifically designed for financial reporting purposes. Many of these have severe design deficiencies and antiquated technology. This leads to lack of accountability, lost audit trails and summary level reports containing inaccurate and meaningless data.

The problem could be materially alleviated by leading edge technology that integrates image and electronic based data entry using *Distributed Process Architecture*. These would link with *Multi-dimensional, Relational Databases* through advanced telecommunications techniques. While this sounds complicated, in fact such systems are in place for financial and management control in the private sector and the core capability is resident in several operational military systems.

Such an approach can bring together disparate components enabling them to "talk" to each other. It also provides for "*Electronic Commerce*" and accurate image entry through scanning devices which eliminate human error. While the databases are open for access to those with appropriate requirements, they still provide sufficient connectivity to ensure secure audit trails. They also offer feedback loops to local operational levels to assure accountability and useful management information. Such a system also provides the foundation for the use of Commercial Off the Shelf (COTS) application programs used in private sector businesses. These would speed the introduction of necessary systems at a fraction of the cost of custom designed programs.

At this point, we feel the need for a word of cautionary advice relating to systems. They simply are not a panacea that will cure all ills. Waiting for a massive systems rework in the hopes that it will magically produce clean audits is counter-productive, expensive, wishful thinking. Lamentably, there appear to be instances of large, highly expensive centralized systems that may not serve customer needs and eventually may be abandoned. It is far better to pay attention to the fundamentals of good financial management and to correct deficiencies at the base level than to build monolithic, electronic monuments that serve only to speed the compilation of meaningless data.

Having said that, I will return to the theme that a building block approach of proving out and certifying functional and feeder systems linked by modern technology is a workable approach. That, coupled with sequential audits of discrete entities, could provide the basis for achieving an unqualified audit for the consolidated federal government by the turn of the century.

Utility of CFO Reports

Having a clean audit is only the first step. It does not guarantee good financial performance. It only means that systems and procedures are adequate to present statements that reasonably describe the financial condition of the entity. To achieve true value, the reports must be meaningful and provide useful information to assist all levels of management in decision making and improvement of business practices.

While the CFO Survey mentioned earlier praised the utility of the improvement process to produce auditable statements, there was some ambiguity about the usefulness of the reports themselves at the operational level. FEI suggests that a means to enhance utility could be achieved through linking the output of the CFO Act with that of the Government Performance and Results Act. GPRA is operation and mission oriented, the key elements of which can be precisely defined through *Metrics* techniques. The CFO Act through its measurement requirements can provide the assets and costs required to deliver the GPRA desired outcomes through *Activity Based Costing.* Using the dollars required to provide a matrix of desired services as a yardstick, the budgeted financial requirements set in CFO format would indicate the resources required.

It should be noted here that we strongly believe that this effort should include a capital budgeting element distinct from other periodic expense items to give it proper visibility and accountability. Testimony to this effect was presented on March 3, 1995 before the House Subcommittee on Management, Information and Technology of the Committee on Government Reform and Oversight. We would ask that it be included in this testimony by reference. We also believe that the entire federal budgetary process is a good candidate for *Reengineering.* Understanding its evolution as part of the political process, the facts are that key budgetary provisions and the sheer size and complexity of the undertaking are root causes of downstream financial management problems.

By describing and measuring performance elements through *Metrics* and *Activity Based Accounting*, the groundwork is laid for the employment of a host of advanced management techniques. This would include *Benchmarking* and *Best Practices* wherein operations are compared across like activities in other organizations. FEI would urge not only comparison with other government entities, but with the private sector as well, where valuable experience has accumulated in the wake of restructuring and downsizing in recent years. These tools can be used to determine the true *Value Added* by a service from the perspectives of the customer. Similarly, it is then possible to define and measure those elements of activity known as *Value or Cost Drivers* that are most influential in determining operational efficiency and associated costs.

Having identified and examined those elements it would be possible to engage in systematic *Business Process Engineering* to determine the most efficient and cost effective means to deliver the required service. A long look should be taken at the way the private sector delivers similar services. How does FedEx run its complex multi-modal collection and distribution system? How does Morgan Stanley manage funds? How does Travelers process insurance claims? How does American Airlines maintain their aircraft? These are services almost identical to those provided by the federal government. Gaining this type of perspective and the relative cost would be a good start to the *Change Management Process* for internal improvement or as the rational justification for outsourcing. In particular, we urge that this be undertaken in business-like activities such as DOD's Defense Business Operating Funds (DBOF), financial asset management and the delivery of financial services.

Through this systematic approach, the CFO financial reports become an integral part of a management improvement effort and act as the scorecard on achieving operating objectives in the most efficient and cost effective manner. In this way, the CFO reports emerge as more than a static picture of financial position, but are transformed into a dynamic focusing agent bringing together strategic planning, budgeting, operations management and accountability. This will yield enhanced Congressional oversight, more effective authorization and appropriation in the budget cycle and more visibility on the workings of government for constituent taxpayers.

Continuing Guidance

To sustain the progress in financial management improvement, we at FEI would encourage the continuing support and guidance of the various organizations and committees that are responsible for the oversight and direction of financially oriented functions of the federal government including this Committee at the forefront. While the department and agency CFOs are on the firing line, much can be done to assist them in their ongoing effort.

Without detracting from the outstanding effort to provide direction, we would encourage expansion of interpretation of the accounting and audit standards that are the underpinnings of financial management. Some of the conceptual issues raised by FASAB require increased guidance for the benefit of the practitioners in the departments and agencies. As we found in struggling to help the Air Force with their contingent liabilities problem, there is a paucity of detailed direction available. We are also aware that standards and guidelines for *Valuation and Materiality* issues are also in order. We would encourage the CFO Council to poll its constituents as to areas where additional guidance is indicated. FEI would be pleased to assist in applying private sector perspective to this effort to the degree possible.

We would also encourage the CFO Council to continue its effort to propose streamlining and integrating the myriad laws and regulations that pertain to financial management. Our impression from CFO's and other senior financial managers is that an overhaul and consolidation is very much in order. It must be emphasized that we are not calling for a rollback on providing direction, but are suggesting a long look at the overall picture from the perspective of the cost and workload impact on practitioners in the field. We would also advise that the end users of the information requested by the regulations be identified and their endorsement of the necessity to continuing provision of such information be obtained. We, in the private sector, are all too familiar with stories of the perpetuation of forms and reports that are no longer relevant and where those who originally requested them are long gone. We hope that this Committee would support such an effort.

An observation is perhaps now in order on the direction of the massive audit process leading to consolidated financial statement for the entire federal governments. In the past, the work of federal auditors was in large measure oriented to operations audits as distinct from financial audits. Thus, we are confronted not only with an audit process of unprecedented size and complexity, but one conducted by auditors who, in some instances, are confronting new challenges. No insult is intended here. We of the private sector have been through first audits before and know just how difficult it can be both for CFOs and auditors. We are only suggesting that the task is large and complicated and that some additional assistance is in order. We would recommend to this Committee that consideration be given to augmenting the internal audit effort with that of independent accountants from the private sector with experience in these critical areas at least during the early "ramp-up" portion of the process. We suggest a teaming effort where government auditors work side by side with private sector counterparts to speed the transfer of technology and experience. We recognize that this is a difficult time to propose additional funding, but strongly believe that the future savings will more than justify the investment.

Our final recommendation would be for each department and agency to reach out to the private sector for advice and counsel. Many of us in the commercial world have experienced downsizing, reengineering, reorganizing and the introduction of new financial management technology. The size, scope, complexity and pace of change which have accompanied the CFO Act and the major realignment of funding priorities have created demands for intellectual, procedural and systems resources that have not been resident inside the Beltway simply because there was no prior need.

Now, both practitioners and overseers are struggling with an unprecedented task on an extraordinary time table. We would propose that the private sector assist in this endeavor through establishment of a Financial Management Advisory Board (FMAB) for each of the 24 CFO Act departments and agencies. This would be an independent outside board of senior, private sector financial officers to provide counsel, oversight and perspective to financial management reform efforts. It would offer the department or agency Chief Executive and Chief Financial Officers a fresh, unbiased perspective and the benefit of their extensive experience.

Their first task would be to review the 5 year Strategic and annual Tactical Financial Management Plans we propose as well as Financial Reports and Audits. The initial objective would be to assist in creation of a specific program to achieve an unqualified audit opinion within the prescribed timeframe along with all of the supporting systems and procedures. Additionally, it would offer counsel on the preparation of reports and presentations as well as general relations with key stakeholders. The FMAB would also serve as an Audit Committee to review reports and management responses. Where appropriate, they would offer advice on industry best practices. The FMAB would serve as a sounding board for top executives on all matters of financial management. FEI would be pleased to assist departments and agencies to create and coordinate such Financial Management Advisory Boards which could be recruited from FEI's membership as well as other private sector organizations. We are prepared to move ahead on this initiative immediately and hope this Committee would encourage departments and agencies to avail themselves of this resource.

Conclusion

Looking back on the 5 years since the signing of the CFO Act, there is evidence of great progress. Laws, regulations and guidance for compliance are in place along with skilled individuals to implement them. There is full recognition of the magnitude of the problem, but also high resolve to master the situation. With all this we have a strong foundation and building momentum, yet to achieve the objectives of the Act by the year 2000 will require more than steady, evolutionary progress.

What is needed is a quantum leap over traditional approaches and technology to accomplish major break-throughs in the management of our government. While urging caution against overreliance on expensive, monolithic megasystems as a singular solution, we feel confident that existing capability in modular, scalable, distributed processing and data base management supported by strict attention to fundamental tenets of good financial management can yield prompt, secure progress toward achieving the objectives of the Act.

Finally, we would urge those tasked with managing our government to reach out to the private sector which has learned many painful lessons over the last decade and which is prepared to share its experiences. In particular, we at FEI are ready to provide perspective and advice from the ranks of our top financial professionals and look forward to being of service to our government.

I would be pleased to address any questions you might have at this time.

○

21-793 (88)

ISBN 0-16-053949-8

90000

9 780160 539497