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STATEMENT OF
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BEFORE THE
THE JOINT ECONOMIC COMMITTEE TAIT 00700
UNITED STATES CONGRESS

ON
THE [NEED TO IMPROVE ACCOUNTABILITY
TO REDUCE FRAUD AND MISMANAGEMENT AND IMPROVE
PRODUCTIVITY IN THE FEDERAL GOVERNMENT]

INTRODUCTION

Mr. Chairman, we are here today at your request to discuss the important topics in your letter of May 22, 1979. Specifically, I will discuss the problems of fraud, mismanagement, particularly in the area of financial management, and the need to improve productivity in carrying out Federal programs. We in GAO believe that these issues are related in that it is in the absence of accountability that fraud, mismanagement, and declining productivity can continue unchallenged.



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Accountability may be considered a clear responsibility for producing at the lowest cost the goods and services necessary to effectively accomplish an organization's mission. In business, managers are held accountable by the profit and loss statement. No such mechanism exists in the Federal Government and agency revenues do not depend on effective performance. Therefore, it is essential that a mechanism be established that holds Federal managers accountable in the same manner that a profit and loss statement holds business managers accountable.

Much has been heard in recent months about fraud in Government as well as numerous charges of waste and mismanagement. The effect of waste and mismanagement is in part demonstrated through low Federal productivity. Federal Government productivity improvement recently has been much less than it can and should be.

Based on the statements of political leaders, the press, interest groups and numerous individuals, it is fair to say that there has been a loss of public confidence in Government. "Proposition 13" and similar actions taken by voters in many states attest to this fact. Public opinion polls support this conclusion. Summarizing these polls, a writer in a recent issue of Fortune magazine said, "Not since the days of the Great Depression have Americans been so complaining or skeptical about the quality and character of their country's public performance." He stated that

Americans have lost "confidence that Government can accomplish those things the people want done..." He concluded that "the tax protest is based on a genuine belief that Government can and should do all that it is doing--but much more efficiently." The call, he says, is "not for less government but for better government." This means more accountability for performance. I would like to address how increasing accountability can help in reducing fraud and mismanagement in the Federal Government and improving Federal Government productivity.

REDUCING FRAUD IN FEDERAL GOVERNMENT OPERATIONS

In mid-1976, the General Accounting Office undertook an effort to determine whether Federal agencies had instituted effective policies and procedures for combating fraud that might exist in their programs, whether committed by Federal employees, by recipients of Federal assistance, or by others. This effort culminated in a report to the Congress entitled "Federal Agencies Can and Should Do More to Combat Fraud In Government Programs," (GGD-78-62, September 19, 1978).

Although bright spots existed here and there with respect to individual agencies antifraud activities, we found many problems in the Government's ability to fight fraud.

The Government's financial assistance programs are vulnerable targets of fraud and related white-collar

crimes as are Federal programs involving grants, contracts, and loan guarantees. Identifying the extent, nature, and frequency of these illegal acts, together with strong internal controls and effective audit coverage, are essential first steps to combating and preventing them. Yet the agencies we have reviewed were not doing nearly enough to identify fraud.

How Much Fraud Is There?

No one knows the magnitude of fraud against the Government. Hidden within apparently legitimate undertakings, it usually is unreported and/or undetected. Opportunities for fraud, however, are tremendous when you consider the magnitude of some Government disbursements. For example:

- The Veterans Administration has annual outlays of approximately \$18 billion in support of veteran benefits.
- The Department of Health, Education, and Welfare has annual outlays of approximately
 - \$109 billion in welfare payments,
 - \$10.5 billion in grants to States for Medicaid, and
 - \$3 billion for student assistance.
- Federal procurements in fisical year 1977 were almost \$80 billion, including GSA procurements for supplies and services, and DoD procurements of major weapons systems.

We found that agencies had not established management information systems to deal with the fraud problem. They did not know the amount of identified fraud in their programs and they could not estimate the potential amount of fraud.

Until recently, agencies have not made fraud detection a high priority because their overriding concern has been program execution and emphasis on such program objectives as providing loan assistance. The low priority given to fraud detection leads to passiveness regarding potentially fraudulent situations.

Also, none of the agencies we reviewed have, until recently, designated a focal point responsible for seeking out and identifying fraud. Consequently, they have generally taken a reactive, rather than active, approach to fraud detection. However, a reactive approach is inadequate for detecting fraud, since there is often no specific incident to react to.

In the past, agencies had no assurance that program administrators were referring all suspected frauds for investigation because:

- There were no controls to see that suspicious matters were reported.
- Large workloads hindered identifying suspected fraud by program personnel.
- Employees lost interest in reporting suspected

frauds when follow-up actions, such as investigations and prosecutions, were not promptly taken.

--Many Federal programs are administered by State, local, or private sector institutions, and Federal agencies often unjustifiably relied on those non-Federal entities to identify and report frauds.

In addition, agency investigators often did not have the background, experience, and training needed to effectively detect and identify fraud.

Since our report was issued, the Inspector General Legislation has been enacted and all but one Inspector General have been appointed. While this is a step in the right direction, more needs to be done.

All too often, fraud cases are viewed as isolated, one-time incidents with no attention given to the weak controls that allowed them to occur in the first place. Top management must recognize the need for and take a more active role in making improvements. It makes little sense to establish an Inspector General system to prevent and detect fraud and abuse and at the same time, have an agency management that takes a passive role in these activities and views them as the exclusive domain of the investigators and auditors. In my opinion, the best Inspector General system, the best audit, the best investigating system that can be devised will be of little use if management

does not become an active partner in the process or fails to use the necessary controls.

Establishment of a GAO
Task Force

Last year I established a Special Task Force for the Prevention of Fraud. We have allocated substantial staff resources over the next two fiscal years to carry out the task force work. The major responsibilities of this group are to

- evaluate the adequacy of the management control systems in Federal agencies that are necessary for the prevention of fraud, and
- assess the adequacy of the follow-up corrective actions taken on reports of auditors and investigators.

One effort of the task force has been the establishment of a telephone "hotline." We have received literally thousands of calls since we implemented the "hotline" on January 18, 1979. However, not all calls are written up for further analysis because they are obviously non-substantive or are state or local matters. We try not to be ombudsmen, although such a role is difficult to avoid.

Even with the initial screening, over 5000 allegations were written up. About 64 percent of these cases appear to have substance for either investigation or audit. For example, of

4,559 allegations written up and coded for computer analysis, 2,979 appear to warrant investigation or audit. We categorized about 39 percent as mismanagement and 61 percent as intentional wrongdoing.

Emphasis Should be on
Prevention, Not Detection

Since prevention is GAO's top priority in the fight against fraud, our work concentrates on identifying and getting agencies to correct internal control weaknesses that permit fraud to occur. When systems have been properly developed and are functioning as planned, the possibility for fraud, theft, or error is greatly diminished. Where the systems do not exist, or are not being used properly, the opportunities to defraud the Government and the possibilities of error increase dramatically.

GOVERNMENT MISMANAGEMENT

Government mismanagement is a recurring problem identified in many of our reviews. We consider mismanagement broadly to be the failure of managers to give proper attention to program controls and costs.

The extent of mismanagement in Government is almost understandable given that managers often are not held accountable for program results. However, since Government revenues are not dependent upon effective performance, the need for accountability is particularly great.

One area in which we have found a number of cases of mismanagement is in Federal financial systems. A good financial management system can provide managers with the information needed to conserve, control, protect, and wisely use resources. A weak financial management system can play a large part in causing agencies to

- incur excessive costs to achieve goals,
- overobligate and misuse funds,
- lose control over cash, property, and other assets,
- fail to collect accounts receivable,
- unnecessarily delay collection of receivables, and
- lose control over accounts payable and, as a result, fail to identify and pay debts on time.

Effects of Poor
Financial Management

The lack of effective financial management among other things has resulted in unnecessary Federal expenditures or in failure to collect promptly amounts due the Government. Some cases discussed in GAO reports and testimony include the following:

- the Government needs to do a better job of collecting amounts owed by the public. We identified \$140 billion in accounts and loans receivable owed to the Federal Government. Many of these were past due. We found that most Government agencies did not take prompt and aggressive

action on collecting delinquent accounts receivable nor adhere sufficiently to prescribed collection procedures.

--in nearly 14,000 audit reports of 34 agencies, \$4.3 billion in audit findings had not been resolved. We estimate that about 80 percent of this amount involves potential recoveries from grantees and contractors, including what they either spent for purposes not authorized by Federal laws and regulations or could not support as charges to the Government. The remaining 20 percent involves potential savings in operating costs.

--the financial management system in the Department of Defense for foreign military sales is fragmented, lacks long range planning, and does not have uniform standards. Although applicable law requires full recovery of costs, many weapons have been sold to Foreign Governments at less than cost because the accounting system did not accumulate costs accurately. Billions of dollars of accounting errors, reporting delays, and other serious financial management weaknesses also prevent the Department from meeting its fiduciary responsibility to its foreign customers.

--the Department of Defense could save millions of dollars annually by simply returning excess cash to the Treasury.

These examples provide but a sampling of the problems in the area of financial management. The existence of these problems in financial management was recognized in a May 7, 1979 memorandum from the Director of the Office of Management and Budget to the Heads of Executive Departments and Agencies explaining the Financial Priorities Program. The program is to resolve the major financial management issues facing the Government today, including accounting systems, internal control, audit follow-up, debt collection, and grant accountability. We look forward to working with OMB in this effort.

There are other areas of mismanagement which I will not elaborate on here today except to say that we find that waste occurs because of poor procurement practices, ineffective use of Government-owned assets, inefficient maintenance practices, and similar uneconomical practices.

PRODUCTIVITY IMPROVEMENT

Although productivity has long been recognized as important for a strong national economy, its value in the government sector has largely been ignored. Yet, governments at all levels employ one out of every six American workers. The productivity of government workers is an important factor in the national economy.

Broad measures of Federal Government productivity have been developed for about two-thirds of total Federal employment.

These measures indicate that Federal productivity has been increasing about 1.2 percent per year since 1967, or slightly less than the depressed rates of increase in the private sector.

There are significant benefits to be derived from improved productivity of the Federal work force. If overall productivity could be increased by only an additional 1 percent, 29,000 fewer workers would be needed to provide the present level of goods and services. Two potential changes could result from such an improvement in the use of people. The level of goods and services could be increased using the same number of workers, or the work force could be cut and result in budget reductions.

Barriers to achieving productivity growth in the Federal Government are many: the absence of a profit motive, the diverse missions, the lack of high-level interest both in the executive branch and the Congress, the disincentives of classification standards and the budget process, the lack of incentives (positive or negative) to enhance productivity, the difficulty of developing meaningful measurements for some programs, the absence of specific goals, and the unnecessary regulations and controls that erode the managers' ability to manage. All of these contribute towards creating a climate that needs to be dramatically changed to achieve productivity growth.

The new Civil Service Reform Act goes a long way toward removing many of these barriers. However, we believe that top management emphasis through a focal point is still needed to tie

together Federal productivity efforts. Such a focal point should serve as a catalyst to making managers consider productivity improvement as a normal part of their responsibilities. Further, agencies need a source for management assistance in problem solving or technical guidance for such efforts as establishing agency-level measurement systems. In addition, a focal point can provide a clearinghouse for transferring ideas between agencies.

In our report on the National Center for Productivity and Quality of Working Life (FGMSD-78-26, May 23, 1978), we recommended establishment of a leadership role for Federal sector productivity in either the Office of Management and Budget or the Office of Personnel Management. The Office of Personnel Management has since been given this role. They have subsequently designated an organizational subelement specifically for the productivity improvement task. We think this is a significant step forward.

ACCOUNTABILITY AND CONTROLS
ARE NEEDED FOR GOOD MANAGEMENT

Holding managers accountable for effectively using resources requires that there be tools available for assessing performance. Performance measurement systems such as productivity and work measures, provide tools by which changes--hopefully improvement changes--can be tracked. Further, such measures can function both as a control tool to aid in highlighting organizations where accountability

is possibly being lost, and as a tool which can show whether performance is better in one period than in another.

We have performed and are performing a number of evaluations designed to assess the adequacy of individual Federal agencies' measurement systems. In general, we have found that agencies are not developing accurate measures of performance. For example, in past GAO reviews we have found:

- Work measurement standards are not based on accurate information, nor are they regularly reviewed and updated. Thus, standards reflect inefficient methods of accomplishing tasks, do not provide appropriate information, and are not credible. Also, the standards are not integrated in with other measurement systems which would allow more extensive analysis of work being performed.
- The reporting of work measurement data is generally untimely and inaccurate. Employees and low level managers do not understand the need for accurate information or are suspicious of the consequences. Reporting methods are generally not monitored.
- High level managers usually do not have a sufficient commitment to developing and using work measurement systems, goals and objectives are not clearly defined nor followed. Consequently, the full uses of such a system are not developed.

The use of performance measurement data as a management tool has been very sporadic, dependent mostly on the motivation and commitment of individual managers. This data is needed to set performance goals and show how Federal managers are using resources. We believe there will be continued difficulty in holding managers accountable for funds until performance data is developed and used.

Incentives are Needed
to Improve Accountability

A basic problem in providing accountability in Government is the lack of management incentives to do so. Without incentives, the elements of accountability--internal control and measurement--are weak at best. We firmly believe that any effort to improve accountability in Government must incorporate proper incentives that include requiring the use of productivity data in the budget process and the use of productivity measures in evaluating performance as part of the new system of rewarding Government managers for performance.

The budget process
as an incentive

The budget process, as the lifeblood of Federal agencies, provides the most appropriate method for encouraging management improvement in agencies. However, as the budget process now functions, many agency executives and managers believe that productivity related improvements often result in a penalty rather than a reward. Examples given to us include arbitrary

across-the-board reductions in staffing and reduction of the next year's budget to force continued productivity improvement. Officials in all of the agencies we have contacted gave examples of how budget reviews in both the Office of Management and Budget and the Congress seemed insensitive to what agencies believed were innovative proposals to increasing productivity. To them, the distressing message was that genuine efforts at improving productivity were often met with, at best, apathy or, at worse, arbitrary budget cuts.

This management environment can be significantly improved by providing meaningful incentives to agency managers. This will require an attitudinal change about the significance of efficiency and good management. The change in attitudes must be reflected in the budgetary process--both at OMB and in Congress--and at the individual employee level. Without attaching real importance to programs designed to improve management, those programs are likely to fail.

Examples of appropriate incentives would include providing organizations with a share in savings produced through productivity improvement and providing managers with flexibility to reallocate staff based on productivity gains.

Linking pay to performance
as an incentive

If an organization's goals and objectives are linked to manager's rewards, managers will make specific efforts to improve performance. This was clearly shown in our examination

of 13 agencies, of which only two related their incentive awards to organizational goals. Even though most of the 13 Federal activities had established organizational goals, and further, had management information systems which related actual performance to organizational goals, these organizations generally did not hold managers accountable or reward them on how well they achieved their goals.

In contrast, incentive plans in private companies are linked to company goals and start at the top where decisions are made, and then filter through the management structure. Generally the goals for top managers involve company profits and rates of return. These managers are eligible for incentive awards based on how successful the business is in meeting its goals and upon their personal contributions to the success.

Many case studies have been documented of Government activities and private sector companies obtaining significant productivity increases through the use of an incentive awards program. One Department of the Navy activity we reviewed is a good example of the productivity gains that can result from an effective incentive awards program. Low productivity, leave abuse, high turnover, and low morale among data transcribers were serious problems at a West Coast naval shipyard.

The Navy installed a system to identify and award employees whose individual performance exceeded normal expectations. During the first year the new incentive program was used,

productivity increased 18 percent. In addition, overtime requirements which had previously averaged 54 hours per week were virtually eliminated and a significant work backlog was eliminated. Because of the improvements at the first shipyard, the program was implemented at other West Coast shipyards with the same positive results. The Navy is currently trying to implement a similar program for all installations employing data transcribers. They have projected minimum annual cost savings of \$920,000.

Although there is a direct and frequently measurable relationship between an incentive program and an organization's productivity, incentives alone will not bring about higher productivity. Incentives obviously are not a substitute for good management; rather they are part of a management system's approach to obtaining higher productivity levels. But we believe it is equally incorrect to assume that an effective work force or higher productivity levels could exist without having an effective incentive awards program.

Conclusion

In conclusion, I would like to emphasize that the recurring theme in the problems of Government fraud, mismanagement, and declining productivity is the lack of accountability at all levels of Government.

Instituting good management systems, which include performance measurement, can greatly increase accountability in Government. In order to make these systems effective, though,

managers needed more than a vague concern for better Govern-
ment; they need incentives that directly affect them on a daily
basis.

The recent actions by the executive branch to reduce waste and fraud and improve management are encouraging. The establishment of the Executive Group to Combat Fraud and Waste in Government and the Presidential Management Improvement Council highlights the significance the executive branch attaches to these issues.

The Civil Service Reform Act of 1978 is a positive step in increasing manager accountability and relating pay and awards to employee performance.

While these efforts are in the right direction, they do not alone provide the needed change. Much will depend on the future work of the Office of Management and Budget, the Office of Personnel Management, ^D the Congress and, of course, individual agencies. *DLG, 00925*

We believe that the Office of Management and Budget should

- require productivity data to support agency budget requests,
- provide departments and agencies with incentives in the budget process to improve management,
- identify management issues for the attention of departments and agencies, and

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--provide support for agency management improvement efforts.

The Office of Personnel Management should

--insure that agencies have quantifiable performance measures in their performance appraisal and incentive awards programs to provide the proper link between pay and performance,

--provide technical assistance to departments and agencies in the development of performance measures.

The Congress, like the Office of Management and Budget, should consistently require that departments and agencies support budget requests with productivity data and encourage and reward those departments and agencies that demonstrate good management.

It is also up to each individual agency to take steps to improve its management practices and manage its resources effectively, free of waste, fraud, and inefficiency.

In addition, we in GAO intend to give these efforts our top priority.

Fraud, mismanagement, and declining productivity are important problems facing the Federal Government. Fortunately, the solutions to these problems appear to be well within our grasp if a concerted effort is taken to solve them.

Since your hearings yesterday focused on private sector productivity, I would like to submit to the record a list of our completed and ongoing work in the area.

This concludes my statement. I would be pleased to answer any questions the Chairman or members of the Committee may have.

COMPLETED AND ONGOING WORK BY THE
U.S. GENERAL ACCOUNTING OFFICE
ON
PRIVATE SECTOR PRODUCTIVITY

Completed work

- Manufacturing Technology--A Changing Challenge to Improved Productivity (LCD-75-436, June 3, 1976).
- The Federal Role in Improving Productivity--Is the National Center for Productivity and Quality of Working Life the Proper Mechanism, (FGMSD-78-26, May 23, 1978).
- Development of a National Productivity Clearinghouse, (FGMSD-79-4, December 12, 1978).

Ongoing work

- A productivity assessment of the shoe industry.
- A productivity assessment of the coal industry.
- Developing legislation to establish a national productivity policy.
- A study of the feasibility of automating the Patent Office to enhance the patent process.
- An assessment of the Department of Labor's quality of working life programs and their effect on productivity.
- A study of productivity sharing plans in the private sector and the effect the wage and price guidelines have on them.

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- An assessment of the availability and constraints on venture capital formation and the impact on productivity growth.
- A review of the capital formation process.
- A review of Federal Government activities in providing trade and production data to Federal and private users.
- An assessment of the potential for space manufacturing.
- A study of the present system of developing national measures of productivity by the Federal Government.