JFMIP

The Proceedings of the 19th Annual Financial Management Conference

Management Control

in the 90s

19th Annual Financial Management Conference

Monday, March 5, 1990
Grand Hyatt Hotel
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Contents

Foreword

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The Joint Financial Management Improvement Program (JFMIP) sponsors an annual conference to address current issues in financial management policies and practices within the government. On March 5, 1990, the 19th annual Financial Management Conference was held on "Management Control in the 90s--A New Agenda." As part of JFMIP's mission to disseminate this information and to enhance the spirit of cooperation among financial managers, we are publishing the Conference proceedings.

The keynote addresses were presented by Robert Glauber, Under Secretary of the Treasury for Finance, and Senator John Glenn. Under Secretary Glauber highlighted financial management and related economic issues from the Treasury's perspective, while Senator Glenn discussed management control initiatives and the status of the proposed legislation for Chief Financial Officers in the federal government. Their speeches can be found in Chapter 1. This chapter also includes an address by Jack Kemp, Secretary, Department of Housing and Urban Development, which was presented by videotape at the Conference.

Two of the JFMIP Principals--Constance Newman, Director, Office of Personnel Management and Charles Bowsher, Comptroller General of the U.S.--gave brief remarks during the luncheon session. This session was highlighted by the presentation of the Donald L. Scantlebury Memorial Awards to two outstanding executives for distinguished leadership in financial management. The awards speech given by Fiscal Assistant Secretary Gerald Murphy, who is Chairman of the JFMIP Steering Committee, and the luncheon session remarks are presented in the second chapter.

The three panel sessions covered financial statements, accountability for government resources, and prescriptions for systems success. Summaries of these sessions are found in Chapter 3.

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Chapter 1

Opening Remarks

Virginia Robinson
Executive Director, JFMIP

Good morning. I am Virginia Robinson, Executive Director of the Joint Financial Management Improvement Program. It is indeed a pleasure to welcome you to our 19th Annual Financial Management Conference. I am delighted to see such a good turnout today. My idea of a good turnout is approximately 700 handsome and alert faces at 9:00 a.m. on a Monday morning at a JFMIP conference.

We have excellent representation here today. I understand that in addition to the representation from a lot of federal agencies, we have good representation from the private sector and a number of representatives from state and local government as well. I have not seen all of them yet, but I understand that we have the Auditor General of Michigan, a budget official from Maryland, and finance and budget officials from the State of Massachusetts. I would like to welcome all of you.

One other thing that I noticed this morning is that we do have a few new faces in the audience. Many of the people who are here are accustomed to coming to our JFMIP conferences as a part of the educational tradition in Washington. But to those of you who are at a JFMIP conference for the first time, I would like to extend a special welcome. I know that some of you have made a special effort to start getting involved in training events and participating in conferences such as these. I do welcome that and encourage you to continue that kind of participation.

There is one special meeting that took place since our conference last year that I would like to mention to you. Last September we had a special meeting of our four JFMIP Principals (three of whom are new). I consider that a momentous event, since it is not an easy accomplishment to get the Secretary of the Treasury, the Director of the Office of Management and Budget, the Director of the Office of Personnel Management, and the Comptroller General of the United States in one room at the same time. They met to share information on past activities and to provide future direction from the perspective of the central agencies.

I was very pleased that their agenda did coincide with a number of the things that we do have under way. The emphasis in that meeting was on financial systems, the improvements that we need to make in that area, the chief financial officer, and improved reporting and much of the work that we need to do in that area. You will notice that much of our program today, as well as our JFMIP projects and our publications, center around those topical areas.

You probably noticed at the registration desk that we have a number of publications that are available for you. Those of you who remember, we have gone 2 years now saying that this is our 40th anniversary, and I should explain how we can have more than one such anniversary. The Joint Program really started in 1948, but the legislation officially establishing the

Joint Program was passed in 1950. So we started the celebration in 1988; worked on the publication in 1989; and it is now available for you in 1990.

Within the next 3 months, we plan to issue three major reports from our projects in the Joint Program. While we will not have those reports available until about 3 months from now, we do have forms available at the registration desk so that you can get them, and any other publications that we issue, if you leave your name and address at the desk. I do want you to be aware of what is on the agenda and what is coming down the pike within the next 3 months.

We will have a draft report on our standardization of financial information project. I know you have heard about that one before. I hope you have read about it in our quarterly news bulletins. We expect that project to highlight the standardized reporting requirements for the Department of the Treasury and the Office of Management and Budget. A key part of that report will also be terms used in financial management and it is our hope, after the issuance of that report, that this will become standardized terminology used in financial management across government.

The second report that we expect to issue within the next 3 months is the standardized payroll/personnel system requirements for the federal government.

The third one is a training report for accountants. We have a lot of interest in training these days, and I do hope you will hear a little about it when the Director of the Office of Personnel Management will discuss briefly human resources issues later this afternoon. I want to call your attention to this report, because I want you to be aware that it is just the tip of the iceberg. We expect eventually to have training reports for other areas of the financial management disciplines in the future.

We call the accountants' training report to your attention especially because of some of the things that you will be hearing today. We have a special need to have emphasis put on training at this time. We are hearing a lot and reading a lot about the activities in the Department of Housing and Urban Development, the Internal Revenue Service, and other areas; and one of the things that we seldom hear asked is what is the level of training that is available to the people who are charged with carrying out those very complex assignments. We want to commend to your attention that we are working very much in this training area in the hope that others will develop a similar interest so we can see that we have training available for our people.

Now, you are going to hear five major topics today. From Under Secretary Glauber you are going to hear some new and interesting things from the Treasury perspective. We typically hear quite a bit about financial systems from Treasury. He has responsibility for economic policy, tax policy, and other areas.

We are also going to hear about Chief Financial Officers' Legislation, financial statements, accountability for government resources, and financial systems.

I should mention that there is a common thread; there is a bottom line running through those areas. And that common thread is the need and the emphasis on the kinds of talents it takes to implement the activities and responsibilities that are associated with those issues.

Although we talk frequently about the complexities and the challenges that we have in government, I mentioned earlier that we seldom talk about qualifications and the training of the people who are charged with carrying out those very complex responsibilities. Frequently we hear that it is important and desirable to run the government like a business. My hope, when you leave this conference today, is that one of the things that you will take with you is that it would certainly be desirable for us to emulate a certain aspect of that comment about running the government like a business. What I hope that aspect will be is a recognition of how beneficial it would be if we could run the government like a business from the standpoint of training the people who have to do the work. We simply would not permit our businesses, our corporations and other firms to operate with the level of interest in training that we do tolerate in our government today.

It is my distinct pleasure now to introduce one of our keynote speakers, Under Secretary of the Treasury Robert Glauber.

Robert Glauber
Under Secretary of the Treasury

By training I am a school teacher and I am flattered that you invited me to talk to you this morning. Just as you are today beginning this last decade of the century by thinking what needs to be done now to get yourselves in position to deal with the challenges of the 21st century, we are doing the same thing at Treasury. We see that what we set as an agenda at the beginning of these last 10 years is going to be the issues that carry us forward, hopefully, to position ourselves and help position U.S. industry for the competitive challenges that they are going to face in the future.

Let me just read to you a couple of paragraphs that my boss, Treasury Secretary Nicholas Brady said in a speech about a week and a half ago: "World events have brought about startling changes in the past year. Who would have guessed a year ago that fundamental political changes and economic reform would sweep through Eastern Europe so quickly? Who would have predicted the striking changes occurring in the Soviet Union?"

If you look for the source of these phenomenal geopolitical changes, there is one common theme--a theme expressed by President Bush in his inaugural address when he said that freedom works. Free people and free markets breed the energy and vitality which produce the highest standard of living for people everywhere. The system of democratic capitalism which we pioneered in America is the beacon which has guided men and women, as they unite against regressive regimes, inspired by the hope of a better life.

"Free people and free markets breed the energy and vitality which produce the highest standard of living for people everywhere."

I think that is important because, as we face the competitive challenges, as our businesses face the competitive challenges which, indeed, are very formidable around the world, and as it becomes clear that we can no longer effortlessly dominate world competitive battles, we really do have a very important advantage. More and more nations have come and are coming to adopt our political and economic philosophies. I think that is very good news because it means that as we enter this competition, we enter it with a home field advantage.

The question I think we have to answer is what does it take to enhance the competitiveness of our corporations as they face this global competitive challenge of the 21st century. As we have looked at it at Treasury, I think it is simple to say this: What we need to do is invest in capital--in human capital, public capital and in corporate capital.

In human capital, clearly, one of the most important things we need to do, and the Bush administration is committed to doing, is to strengthen our educational system. Our dropout rate is roughly 25 percent. It is impossible for us to win this kind of competition if a quarter of our players are just simply left on the bench. We need to push even harder than we have toward a drug-free society. Drug dependence puts many of the best of our potential workers on the sidelines and it simply saps our human capital.

"What we need to do is invest in capital—in human capital, public capital and in corporate capital."

Second, we need to build public capital. We need to invest in clean air, a clean environment and a modern and efficient infrastructure.

Third, and the issue which is really closest to the Treasury and its agenda, we need to build corporate capital that is necessary for the 21st century. If we are going to do that, it is critical that both managers and investors have a long-term perspective as they make their decisions. We simply cannot get where we need to go focusing one quarter ahead at a time.

So let me talk a little bit about what we are thinking about and trying to do to encourage this long-term way of thinking which those of you who have read the business magazines know that it is really a fundamental concern of Secretary Brady.

I think the first thing we can do to encourage this long-term thinking is to lower our cost of capital. To lower our cost of capital, I think the first thing we have to do is reduce the federal budget deficit. Doing that is going to lower interest rates and probably be the single most important thing we can do to lower the cost of capital.

As you know, the Bush administration is committed to lowering that federal budget deficit, and to do it by cutting spending rather than raising taxes. In our view, the only lasting way of getting there is by cutting spending. It is just a historical fact that most dollars from increased taxes will surely go not to reducing the deficit, but to building bird sanctuaries in West Virginia.

"I think the first thing we can do to encourage this long-term thinking is to lower our cost of capital. To lower our cost of capital, I think the first thing we have to do is reduce the federal budget deficit."

With the leadership of President Bush, so far I think our record is very good. We managed to get within the Gramm-Rudman-Hollings targets last year. Even though it took a commitment of accepting sequester, we did it last year. We have put in this year a budget which meets the $64 billion target. If necessary, the Administration will accept sequester again. As I say, this is the single most important thing I think we can do to cut the cost of capital.

There are other things we can do and there are other initiatives we have taken. We have introduced a capital gains tax plan which reduces the capital gains tax rate and reduces it more the longer the person holds a capital asset. It is a reduction of 30 percent for assets held 3 years or more, 20 percent for 2 years or more, and 10 percent for assets held 1 year or more. By doing that, we are again underlining the importance of long-term thinking.

The third thing we can do, and we are committed to doing, is to increase the personal savings rate in the U.S. As you know, the personal savings rate in the U.S. has dropped dramatically and it has dropped to a point where we now lag behind most of our foreign trading partners by as much as 50 percent. The personal savings rate in the U.S. is less than half the personal savings rate in Japan and lower than virtually all of our foreign trading partners. It is also lower than it has been historically in this country. Back in the 50s, 60s and 70s the personal savings rate, that is, personal savings as a fraction of after-tax income, was a little bit over 7 percent. During the 80s it has been just a little bit over 5 percent. We simply have to save more and we have to encourage people to save more.

To do that, the Administration has proposed two important initiatives. One is the family savings account plan, which is a plan which will allow people to take money from after-tax earnings, put it into an account for no longer than 7 years, if they choose, and take the money out at the end completely tax free. This is a simple, straight-forward way of saving; a tax incentive could do it. It does not have the ill liquidity characteristics of an IRA plan where money has to be held until age 59.5 to get the tax-deferred treatment. We think it is an important initiative. The polling that we have taken so far suggests that it is and we hope that we can get this passed through Congress in very much the form we have proposed.

The other initiative is an enhanced version of the IRA plan currently in existence. As you may know, right now to withdraw money from an IRA, a participant has to pay an excise tax of 10 percent. That tax will be waived on withdrawals of up to $10,000 if those funds are used to purchase a first-time home. With the cost of homes going up to the point where they have, they are in many cases almost out of reach of many individuals, many families. This is a plan which at least will help put them back in reach.

These are proposals which are in the President's budget. They are the first installment on our commitment to lower the cost of capital. We have other installments down the road. One of them that is sort of near down the road is to try and develop a plan to eliminate the double taxation of dividends. As you know, corporations can deduct interest but they cannot deduct dividend payments, with the result that we favor the use of debt over the use of equity in the way corporations finance themselves. This incentive to use debt rather than equity has not been lost on corporations. Good financial managers, like yourselves, make the obvious conclusion, that is, to substitute debt for equity. The result has been, on the average, about $100 billion of debt being substituted for equity in corporations over the last 3 or 4 years each year. This has led to increased leverage in corporations and increased financial instability in those corporations.

We believe that it makes no sense to tax interest once but the dividends twice and we are working on proposals which will right this imbalance, which will lead to even-handed treatment of debt versus equity in corporate capital structures. We will have a report out later in the spring which will at least begin discussion on this issue.

If we can accomplish these various initiatives, I think the payoff will be reduced cost of capital. The payoff will be more investment, greater growth and a higher standard of living for all Americans.

Beyond that, there is another area where I think we can make a contribution to building capital. That is, to get investors also to look at the longer term rather than to focus on quarterly financial results. Here, again, there are a number of steps that can be taken. First of all, the capital gains tax proposal clearly will do this. If investors receive a greater exclusion on their taxes the longer they hold investments, they are going to clearly have an incentive to hold for the longer term rather than the shorter term.

We can also look toward our pension funds. In this country we have the most fully developed pension fund system in the world. These pension funds are an obvious source of the kind of patient capital, the kind of long-term investment that we so badly need in this country. After all, pension funds have as their liabilities long-term liabilities. It is perfectly sensible for them to be long-term investors. Moreover, it is increasingly clear to most of them that they are simply too big to spend a lot of time trying to pick individual winning stocks; that what they really badly need is corporate relations which will allow them to invest large amounts of money over long periods of time.

But that kind of patience in investment also requires participation. Simply put, many investors, including the large institutional investors, have felt that their voices are not sought by management, much less heeded. The consequence has been that a whole series of corporate raiders have increasingly designated themselves as the policemen of capitalism.

Now, it probably is true that having such policemen on the beat is better than having none. But this, surely, is not the best kind of corporate governing system to which we can aspire. This is a confrontational corporate governing system, not a cooperative one. It leads to revolutionary changes, not evolutionary changes.

We think we can do better and we are looking at this issue. We have taken some steps in this direction already at Treasury. We have a joint responsibility for ERISA, the law that governs private pension fund investment. The Secretary has already made clear that ERISA does not require pension fund trustees simply to take a tender offer merely because it is above the current stock price.

We will also, in the near future make clear some other issues under ERISA. For example, that active participation by pension funds in the management of corporations through communicating with boards, through communicating with management, is completely consistent with their obligations as fiduciaries.

I think there is more that can be done and we are going to continue to examine this and speak out on it over the next months. I think that perhaps some changes in the way nominating committees and boards are constituted would make sense; some changes perhaps in the way directors are compensated. For example, to compensate them more with common stock rather than cash would be a way of aligning their interests more directly and firmly with the shareholders.

Finally, in order to encourage investors to take a longer-term view, it is our view that we still need to make fundamental reforms in the way the stock market operates in order to bring investors back into the stock market and related markets. This is an issue that Secretary Brady has been greatly interested in since he was Chairman of the Reagan Task Force on Market Mechanisms, which was empaneled to study the 1987 stock market break.

Here I think there are fundamental market mechanisms which need to be strengthened and made more consistent in order to reduce the excess volatility which has come to dominate the markets. We need to harmonize stock index futures, stock options, and margins. We need to coordinate circuit breakers which have been developed to deal with these marketplaces.

I think these are very important steps because we concluded in the 1987 study, something which is pretty obvious but seems not to have really confronted people before. That is, market for stock options and stock index futures are really one market. They function together. They operate as if they were one market. The problem is that in this country we do not regulate them as one market. We have the Securities and Exchange Commission (SEC), which has responsibility for stocks and stock options, and we have the Commodity Futures Trading Commission (CFTC), which has responsibility for futures, including stock index futures.

What is interesting is that every other country around the world has one regulator where we have two and I think we pay a real price for this fragmentation. We pay a price in terms of conflicting market mechanisms. We pay a price in less effective enforcement against manipulation, and we pay a price in creating roadblocks to innovation.

There are a number of alternatives to dealing with this, going all the way from full-scale merger of the CFTC and the SEC, down to some individual piecemeal kinds of fixes to deal with margins, to deal with enforcement, to deal with circuit breakers, to deal with jurisdiction and innovation.

The problem that stands in the way of any of these fixes is that Congress is very jealous of its jurisdiction. As you probably know, stocks and options--the SEC is the jurisdictional responsibility of the agriculture committee. That has to be worked out. But, frankly, I think if we do not do anything to deal with this regulatory fragmentation, when we have the next big down-market, and I think that will come at some point, everybody is going to be very embarrassed that they have not done more to deal with this problem. So I think we have to do something, and we have to do it soon if we are going to reassure investors and bring them back into the market which, again, is a way of furthering long-term thinking. That is, briefly, a piece of the agenda of Treasury that deals with investors, corporations and the need to stimulate competitiveness.

Frank Hodsoll
Executive Associate Director
Office of Management and Budget

It is a great pleasure for me to be here with you. It is a particular privilege to be able to introduce our most distinguished keynote speaker. Before doing that, let me just join in extending my own congratulations to the winners of the Scantlebury awards this year. I had the chance, over the last year, to work extensively with Bill Kendig, and I can say from OMB's perspective that his pioneering work on internal controls has helped us all move forward significantly.

One of the first speaking engagements I had last year was at the JFMIP conference. At that time, I asked my staff what it was that I should say to this distinguished gathering, and they said that what I should point out was that there was significant progress in making financial management improvements, but there was more to be done. I have been at OMB for a year and what I would like to say this time is that there has been progress, but there is much more to be done.

What is significant about this past year is that we have identified and zeroed in on at least a few of the needs in financial management. In this respect, we have been assisted, not only by the General Accounting Office and others in the Executive Branch, but also by Senator Glenn's Committee on Governmental Affairs. It seems to us that financial systems are the key to good management controls and that improved financial systems are needed to provide managers at all levels of government quality information to manage and oversee programs that provide services to the public. Every major agency has a program underway to improve its financial systems.

After looking at some of the statistics today, I noted that in the past we had over 400 systems, many of which were incompatible. I noticed that in the budget we reported that we are down to 235. Yet, only yesterday, we discovered at HUD that there were 69 additional systems that we had not counted, so we are back up to 314. It makes me very nervous because I wonder what is going on at all the other agencies if this is true at HUD.

However, we are making some progress. For the first time in a number of years, the JFMIP Principals met last fall to discuss what needed to be done. One of the things that we made an agreement on, which we now have to implement, is to adopt and implement the core systems requirements that were brought forth by the JFMIP.

In the area of financial management, we need the help of everyone here. We need the help of the Congress, the GAO, the President and all of the Executive branch. We need to be able, as Connie Newman eloquently stated, to attract and retain qualified financial managers. We need systems that produce accurate and eventually auditable data. We need internal controls that anticipate and prevent misuse of government funds. We need uniformly applied accounting standards and principles and we need auditable financial statements in critical programs and agency areas. We need to do this now.

I was reminded in talking with Jerry Murphy and our steering group on CFO legislation of some of the previous reform efforts such as the "Reform '75" and "Reform '88" programs. We should dedicate ourselves to making changes, for if there is something that could be called "Reform '90", it must be something that is accomplished at least by 1995, as opposed to continuing the same old problems.

Now, I would like to introduce our distinguished keynote speaker, Senator John Glenn, who will address CFO legislation.

Senator John Glenn

I would like to introduce two people with me today, the staff director of the Governmental Affairs Committee, Dr. Len Weiss, and Bob Coakley, who have done a lot of work on CFO legislation, particularly with Chuck Bowsher over at GAO, and will be continuing to work on this CFO legislation. If you have some suggestions on this CFO legislation or financial management area, give one of them a call. We are soliciting your ideas on this legislation. We do not feel we have all the wisdom in the world up on Capitol Hill all the time, just most of the time. But if you have suggestions, we would appreciate your getting in touch with me. I say that with all sincerity.

The theme you have chosen, "A New Agenda for Management Control in the 90s," is very appropriate and timely. In my view, the federal government is on the precipice of an important management reform movement, but when I went through the speech a short while ago, I think if we put more true words to it, that would not be the right word--precipice. That indicates that we are about to dive off into something that may have some very bad portend to it. I would say a better choice of words might be that we are on the verge of, we have the opportunity to, we may move to new heights if we do this; or probably the way I would express it is that we will stop being stupid and move into the 21st century.

So I am supporting the movement that you talk about with efforts to develop legislation to establish a CFO, a chief financial officer, for our government. The thrust of this legislation will be to establish the organizational structure, the powers, and the master plan needed to bring about reforms in the financial management of government programs.

The need for better financial management is not a new subject for this audience, of all audiences that we could get together. Most of you have toiled in this field. You have been workers in the vineyard for a long time--much longer than I have.

Let me strike a few historical notes, and I will speak to the unusual opportunity I believe we have immediately before us. The Joint Financial Management Improvement Program, JFMIP, is celebrating its fortieth anniversary. Secretary of Treasury John Snyder, Comptroller General Lindsey Warren, and Director of the Bureau of the Budget Jim Webb, whom I was long associated with in NASA, started this organization in 1949, after World War II, to promote governmentwide improvements in financial management. In the mid-60s, what is now the Director of the Office of Personnel Management joined the JFMIP and since that time a lot of water has flowed over the dam. I personally want to take this occasion to commend JFMIP for its contributions to financial management over the years. As Chairman of the Governmental Affairs Committee in the Senate, I am particularly sensitive to the mission of trying to change and improve operations governmentwide, across the board.

In the Executive Branch, each agency has its own view of how the nuts-and-bolts operations should be done. Each agency becomes best in its own practices, and there is a natural resistance to viewing the Executive Branch as a whole.

Similarly, in Congress, each time the Chairman of Governmental Affairs steps forth with a governmentwide approach to the economy and the efficiency of government programs, which are our two main roles--organization and efficiency of government, every other committee chairman casts a wary eye--the old turf fight. So I have a certain affinity for JFMIP's mission.

Another historical observation I want to make is that the Committee on Governmental Affairs always has a strong interest in the work and achievements of JFMIP. This is due to the common beginnings of the Committee with the principal members of the Program. The Committee was created in 1921 to help coordinate the expanding budget needs of other committees and to address the need for an executive budget.

The first bill considered and passed by the Governmental Affairs Committee was the Budget and Accounting Act of 1921. That Act created the Bureau of the Budget and the General Accounting Office from financial management components of the Department of Treasury.

Among other important tasks, JFMIP has served as a continuing forum for common interests of the separated parties. For example, this organization was essential to the Budget and Accounting Act of 1950. It contributed significantly to the Financial Integrity Act of 1982. Over time there have been ebbs and flows to the intensity of this forum, and I want to commend JFMIP for its persistence. Persistence and sustained commitment are perhaps the most important factors to bring about change. Without them, things just do not happen in our nation's capital. The work of JFMIP is to be applauded. Remember, life really does begin all over again when you turn forty, as this organization has.

"Congress will respond to the significant early warning signals being sent by the high risk lists."

Let me turn to the here and now. Over the past several Congresses, Senator Roth, the ranking minority member on my Committee, and I have proposed bipartisan legislation to establish a Chief Financial Officer for all of government, and for each department and each agency. Last week the Committee marked up a Department of Environment Elevation Bill which contains a statutory CFO. While Congress has agreed to a statutory CFO for the new Department of Veterans Affairs and for HUD, we have not succeeded yet in attracting congressional support, beyond our Committee, for a comprehensive bill, a more inclusive bill.

Last year's events, coupled with the Committee's recent hearings on serious management problems in government, lead me to believe that this session of Congress presents an unusual opportunity to pass chief financial officer legislation. As is common to reform movements, crisis and turmoil have brought us to this point. Recall that even with the momentous events in Eastern Europe, the year 1989 left us with a pervasive domestic message as well. There is a growing feeling that we need to act and to put our house in order.

How many more HUDs are out there? That is the nagging question that the year 1989 has left hanging over us. I understand Secretary Kemp addressed you this morning by videotape. He probably noted to you that the HUD scandal came as a surprise to the new Administration and the Congress. The President and his cabinet knew they had a savings and loan disaster to manage, and they had continuing problems with the procurement scandals at the Defense Department. They were also aware of the big issues surrounding the budget deficit, but they did not know about the hemorrhaging at HUD.

"We must take steps to assure ourselves that we can prevent future HUDs while we move to correct the problems already identified."

Early warning signals sent by way of the Inspector General and Financial Integrity Act reports were not seen or, if they were seen, they were not heard; if they were heard, they were not acted upon. We have to share some of the blame in Congress, because we had some of those same reports earlier. But we now know that billions of dollars have been wasted and the American taxpayers will have to pay for the losses.

The Governmental Affairs Committee was instrumental in creating the Inspectors General structure. It was established in 1973 as sort of a test program. We applied it to some departments of government to see how it would work. It worked so well, we have now expanded it. Legislation the year before last expanded it, added eight more government entities to that group, and we think that they have done a rather superb job. It has been one of the best experiments in government that we have had in a long time. The IGs have done very well, and I am a strong supporter of them.

We originated the Financial Integrity Act, a law that requires agency heads to report annually on the adequacy of their internal management controls. I and other members began to wonder about what other early warning signals might be flashing. I began to question whether the Executive Branch even has in place the system needed to give early warning signals.

Last September my Committee took testimony from seven Inspectors General on problems in their agencies. The testimony was alarming. The Department of Energy IG described DOE contractors operating nuclear weapons production facilities under contracts so one-sided that once money is spent by the contractor, no matter how outrageous the expenditure, the government simply pays up. In 1989 DOE obligated some $15 billion in overall contracts, an area that may be vulnerable.

The NASA IG testified that NASA is unable to oversee its spending to the degree it should, 88 percent of which goes to procurement. Inadequate contract administration allows subcontractors to reap excessive benefits.

NASA subcontractors are not being subjected to competitive bidding in many cases. In 1990 alone, NASA will spend, in turn, some $11 billion on contracts.

The Labor Department IG stated that Labor has failed to establish a viable criminal deterrence program to protect American workers' pensions, safe work places, and decent wages. He asserted that there is widespread fraud and abuse in programs administered by the Department.

The EPA IG pointed to millions of dollars of assessed fines which were reduced by as much as 90 percent without any rationale. He described EPA programs as forceless enforcement and EPA as a paper tiger with no deterrent effect on those who violate environmental laws. He testified that it was cheaper many times to pay the fines and go right on polluting rather than to stop.

The HHS IG pointed to fraud in the Food and Drug Administration's generic drug approval process, the Medicare secondary payer program, and Indian Health Service. He targeted a complicated procurement in the Health Care Financing Administration (HCFA) to manage prescription drug reimbursements which would cost over half a billion dollars to put in operation, and he predicted that it would not work.

"We believe that consensus among the three central financial—agencies—Treasury, GAO and OMB—is critical for any reform measures to succeed."

These are just some examples. That is a negative approach to it. In October 1989, the Office of Management and Budget Director Darman testified on the Administration's assessment of management problems within the agencies. He was quite direct, and he stated that there are several HUDs looming in the Executive Branch that have not been uncovered. He released what we call high risk lists, which had been developed jointly by the agencies and by OMB. The lists, largely based on the most current Inspectors General and Financial Integrity Act reports, highlight key vulnerabilities in each agency's operations. The entire set of agency lists they put out encompass 106 high risk areas.

In November, Comptroller General Bowsher gave my Committee his assessment of the Financial Integrity Act process and described GAO's evaluation of high risk areas. The Comptroller General was equally direct. He also believes that there are several HUDs looming out there yet to be uncovered, and he announced GAO's own high risk list of 14 targeted areas and concluded, by quoting him, that "Unless something more is done to correct the material deficiencies in management information and accounting systems and material weaknesses in internal controls, major losses of federal funds and the collateral fraud and abuse incidence will continue."

So two different agencies of government--the investigative arm of Congress represented by the Comptroller General and GAO, and the OMB led by Dick Darman and Frank Hodsoll--now have their reports coalesce. They are concentrating on the same areas that we are looking into now.

The Comptroller General asserts that there are at least $150 billion at risk. Underpinning the assessments of both the Comptroller General and the OMB Director is the clear-cut conclusion that as a government we do not have the basic financial management systems in place to really know what is going on. In addition, internal management controls which are in place are just not working many times. The high risk lists amount to best guesses at where the next HUD-type problem might occur.

The single most prevalent theme running through the lists is the material weaknesses of financial controls. Last week Comptroller General Bowsher testified on GAO's three-year audit of the Air Force. The Air Force was chosen as the first of these in-depth service audits, which I believe may be the first audit we have ever had to this degree of detail. The Comptroller General picked the Air Force to be the first service to be audited, because it was believed to be the best managed service. He concluded the Air Force uses inaccurate, unreliable accounting systems to manage assets worth $225 billion; that the cost of major weapons systems, including the B1B, have been significantly underestimated in the Air Force's own financial records. The record-keeping deficiencies have led the service to stockpile $10 billion worth of excess inventory. There are 131 separate accounting and management systems within the Air Force. Tomorrow the Department of Defense and the Air Force will be testifying before my Committee on these audit findings and these very serious issues.

My view is that Congress will respond to the significant early warning signals being sent by the high risk lists. The Committee on Governmental Affairs will be dedicating most of its attention to programs on the lists and to what role chief financial officer legislation can play to help remedy the problems which are being uncovered. My message to you is that the management agenda for the 1990s is to respond effectively to that nagging question of 1989. We must take steps to assure ourselves that we can prevent future HUDs while we move to correct the problems already identified.

Senator Roth and I both believe that the establishment of a Chief Financial Officer for the Executive Branch of government is necessary to accomplish the needed reforms. We believe that consensus among the three central financial agencies—Treasury, GAO, and OMB—is critical for any reform measures to succeed.

We have not as yet reintroduced either of the legislative proposals we sponsored in the 99th and 100th Congress. Instead, this past January we wrote to Comptroller Bowsher, Secretary Brady, and Director Darman and asked them to meet and try to come to a consensus on three key issue areas. The three issues are rather fundamental.

First is the qualifications, resources, organizational location, and responsibilities of the chief financial officers for all of government and for each agency. In addition, we are addressing architecture audit provisions; financial information that is provided to the boss so that he gets the best possible information; annual audits and financial statements and what form those things should take. There are some different thoughts in that particular area. But we want something substantive for this legislation.

Second is the most appropriate means of ensuring the adoption of accounting principles and standards which recognize the unique circumstances of the federal government.

Third is the approach for improving financial information through the preparation and audit of financial statements.

I would add the following thoughts for this audience to consider. Even with strong legislation, the changes will not occur overnight. Sustained leadership over a long period of time will be needed. An organizational structure with clout will be necessary. An effective governmentwide chief financial officer will require, first of all, access to the President. Moreover, as Comptroller Bowsher frequently notes, we still do not have the basic architecture and the central plan that, once in place, both the agencies and Congress can follow.

There will be a need for more congressional oversight than this subject has received before. Presently, we do not even know how much money is being spent on financial systems and how much more new money will be needed to put some of these new controls into place. What is more critical, though, is that we get started and come with a high level commitment from both the Executive and Congress. It will take legislation passed by the Congress and signed by the President to cement the needed partnership.

I certainly look forward to the day when the federal government can say that we have standard accounting systems. The latest OMB figure is that there are 304 different accounting systems in government. A couple of years ago, GAO estimated we had over 400 across government and the figure was still going up. We had not identified all of them. I think there are some 200 major systems now. OMB has identified 304 different accounting systems. Take your pick of any of those figures; it still has horrendous problems, as I am sure you will all agree.

Contributions that the JFMIP made to a standard general ledger and standard data elements are outstanding. But I remain tremendously frustrated and still do not understand why after all this time we still have hundreds of accounting systems that do not talk to one another in too many instances.

We have scheduled hearings in late March to specifically address CFO legislation. I understand that discussions are underway as a result of what Senator Roth and I distributed. We have asked that three of the JFMIP Principals be prepared to testify at that hearing in late March, and we intend to introduce a legislative proposal before the hearings. Let me stress this positive note for the conference: I believe Congress will address and pass chief financial officer legislation. That is what we are working toward this year. Thank you very much.

Secretary Jack Kemp (Address by videotape)

Hello. Thank you for inviting me to your Colloquium on Improving Federal Financial Management. I'm sorry I can't be with you in person, but I welcome this opportunity to speak to you by videotape.

The American Institute of Certified Public Accountants has a respected position in the world of business and government. You have been recognized for long-standing leadership in the realm of responsible financial operations and management ever since the founding of your organization in 1887, an event which I understand marked the birth of the accounting profession in the United States.

Your organization has created and shaped accounting principles and auditing standards. You fulfill a vital role in the business life of our Nation and have extended the range of your contributions and influence to the international business community, as well.

I have taken special note of your call for the improvement of federal financial management and wish you success in this effort, for I believe we share many of the same goals in that regard.

After assuming the stewardship of HUD, I discovered that the Department's management system was severely lacking in the rigorous financial accountability necessary for efficient and responsible operations. Indeed, it was extremely difficult...in some cases, virtually impossible...to evaluate the financial health and effectiveness of many of our programs. This limited our ability to judge whether programs were properly targeted and often left the Department unable to recognize when program funds were benefitting consultants rather than needy Americans.

From "day one," President Bush and I have made it abundantly clear to everyone at my Department, and to everyone we deal with...individuals and organizations alike...that we do not and will not allow HUD's programs to be abused for political purposes or personal gain at the expense of those in need.

I wanted to clean up past abuse and prevent future abuse, so we could fulfill our commitment to use the full resources of HUD to wage war on poverty, homelessness, and despair. With the full support and cooperation of President Bush, I initiated a Department-wide reform...comprehensive changes in program management and financial accountability to "Clear the Decks" at HUD...so we could move forward on an agenda to create opportunities for home ownership, jobs, and hope in our Nation's inner cities and distressed rural communities.

Our reform concentrates on three areas: ethics, management and finance, and the Federal Housing Administration.

Ethics Reform

Under ethics reform, we have established a strict requirement that all consultants and lobbyists representing grant applicants to HUD must register with the Department. Those applying for funds will be required to disclose any fees paid to lobbyists, consultants, and lawyers in connection with their application.

I suspect you will be most interested in the changes being made under finance and management, and under FHA.

Management and Finance

I am creating a new position--Chief Financial Officer--to report directly to me, with responsibility for overseeing HUD's financial operations. I am also appointing a Comptroller for FHA.

Our CFO will have broad powers to develop, maintain, and oversee the Department's accounting, financial control, and cash management systems. The FHA Comptroller will oversee the financial operations of FHA and be accountable for producing annual audited financial statements for our insurance operations on the basis of generally accepted accounting principles.

In addition, I created a task force to identify systemic management problems in 26 major program and financial management activities of HUD. The task force is currently documenting their findings, recommending solutions, and developing an action plan to implement prescribed solutions.

We also have contracted for an independent management firm to identify structural and systemic problems and to recommend comprehensive reforms to strengthen the financial and managerial integrity of HUD's programs.

And, separately, Price Waterhouse is examining and recommending improvements in the financial policies, practices, and controls in HUD's Office of Finance and Accounting.

FHA Reform

Ladies and gentlemen, I don't need to tell you that annual audited financial statements are the most basic of all management requirements...or that insurance operations call for both cash-based and accrual-based records. Well, FHA did produce internal financial statements; but these were done for the most part on a cash basis, not the accrual basis necessary to accurately gauge an insurance operation's condition. Unfortunately, this gave FHA's managers an unrealistically rosy picture, because claims were counted only when they were paid, not at the time of default.

We're requiring...and will publish...annual audited financial statements prepared by an independent accounting firm. These statements will be on an accrual basis, and will be consistent with generally accepted accounting principles. The auditors also will provide a management letter pointing out deficiencies in FHA's financial control and management systems.

Frankly, we never knew on a regional or program basis how we were doing financially. We intend to design management information systems which will produce timely financial results so that managers can regularly measure our performance against defined financial targets. This information will help us insure the proper relationship between cost and benefit in our programs.

There are major improvements in our accountability which I'm sure will help us manage FHA responsibly and efficiently; but financial-statements only tell us history — how we've done lately. We need to understand how we're likely to do in the future under a wide variety of circumstances...we need the kind of understanding good actuarial studies deliver. And we're going to do something about this need, too.

We've commissioned an independent actuarial study which will develop for us a permanent econometric modeling capacity. This modeling capacity will help us test the impact of rapidly changing economic conditions, the effects of proposed legislative initiatives, and the effect of various terms and conditions on the viability of our insurance policies.

Although FHA operates 47 different insurance programs and has over $300 billion of insurance-in-force, it has but one certified actuary. I understand that the Prudential Insurance Company, for instance, has 150 actuaries. Well, we're hiring additional actuaries for FHA, and developing an ongoing review process for all insurance programs.

There are other reforms under way, and we will respond promptly to the need for further steps as events and experience dictate; but, I assure you, there will be no turning back. We're going to see to it that HUD operates responsibly on a financially and managerially sound basis.

We have begun a fundamental redirection of our programs...a redirection which is enabling us to reaffirm our Nation's moral charter to provide affordable housing opportunities and job opportunities for all Americans. I believe the fulfillment of that charter will be achieved through empowerment...helping people to help themselves by strengthening the linkage between effort and reward, and by removing barriers to their economic independence.

Not all of those barriers are imposed at the local and state level; mismanagement of federal programs is an awful waste of public funds and of the public trust. It is a barrier that deserves the same fate as the Berlin Wall. At HUD, we're tearing that barrier down with the powerful force of good financial management.

I know we have your best wishes and support in that effort. And I urge you to keep up your good work in the continuing drive to improve federal financial management.

Thank you and God bless.

Chapter 2
Remarks and Awards Presentation

Constance B. Newman
Director, Office of Personnel Management

"Management Control In The 90s - A New Agenda"—What a fitting conference theme. All aspects of management must recognize the imperative of establishing a new agenda for the 90s or the federal government will not be in a position to serve the public well. Among issues to be on the federal government's agenda are

- How can the federal government increase its productivity? This issue is important for government to address because of the growing demands of this service industry. Also, this issue is important to address because of the environment of tight resources which will not change.

- How can the federal government assure the public that it is managing its business effectively and properly? Unfortunately, much of the general public does not have the confidence it should in the federal government. A few bad news stories of improper controls and improper behavior have colored the way the public thinks about all of us.

- How can government manage a work force of changed demographics? We must plan for the future with the recognition that the work force is aging and that a high percentage of the new entrants into the work force will be women, minorities, and immigrants.

Financial managers are key to the proper consideration of each of the issues I identified. Financial managers, then, are key to insuring that the federal government accomplishes its goals and objectives in an efficient and effective manner. Now more than ever before in the history of the federal government there must be serious and quality attention paid to accounting and financial controls. Now more than ever before there must be serious and quality attention paid to forecasting and long-range planning.

You, the financial managers, have the expertise and experience which will be important to the management teams properly managing today and preparing for tomorrow. It has always been expected of you that you be responsible for the maintenance of the financial records. But in this time of budget constraints your expertise is needed to assist all management in forecasting the costs of operation, in forecasting the impact of technological changes, and in determining the manner in which historical data can be used to plan future operations.

I would like now to spend a few minutes on human resource management, the part of the management equation we must understand at the Office of Personnel Management - the part of management equation upon which we should be prepared to provide leadership in the development of plans and policies.

We must make certain that the government does, in fact, have the "Best and the Brightest" in its ranks. We start by changing those systems that impact on our ability to attract and retain top-notch workers. We must look at how we compensate, both in terms of pay and benefits, how we classify, how and when we train, how and when we recruit, how we evaluate performance, and how we ensure that political appointees and career employees work together effectively.

I think it is clear that this administration recognizes that there are systems problems that need to be addressed, and has taken steps to do just that.

Pay Reform

One system we have currently addressed is pay. "Phase One" of pay reform is already on the table as part of the President's Budget Request to Congress for fiscal year 1991. The provisions indicate change - a new way of doing business, for they

- provide salary differentials of up to eight percent for federal employees in New York, Los Angeles, and San Francisco;
- provide a five percent increase in starting salaries nationwide at the GS-5 and GS-7 levels for college entry-level jobs;
- allow hiring at pay levels above step one in each grade; and
- provide recruitment, retention, and relocation bonuses for critically-skilled workers.

The aim of pay reform will be to make the federal pay system more responsive to diverse and dynamic labor markets, while using scarce payroll funds in the best way possible. The end result we are hoping for is a more marketable, more flexible and more "predictable" pay system for the federal government.

Health Benefits Reform

Another system we are working to improve is the Federal Employees Health Benefits System. On March 1, we sent a proposal to Congress that would accomplish three major goals. The proposal

- ensures informed choices for enrollees in the Health Benefits Programs,
- creates a system that treats employees and retirees equitably, and
- achieves economic efficiency in the overall program.

Specifically, our proposal offers five indemnity packages or the available HMO alternatives for all enrollees. Premiums for these packages would be set on a nationwide basis, and the rates and benefits would be separately tailored for employees and retirees.

The proposal plans to deal with the economics and costs of the system in a number of ways. First, the new system would follow private sector practices in cost containment through contractors who would process claims and administer each separate indemnity package. To deal with the costs of the program, our proposal would stabilize the costs through a number of legislative and administrative actions.

It is important to know that the President in his State of the Union Address committed this administration to a broad-based, top-level review of critical health issues facing the Nation. This proposal to reform the Federal Health Benefits System is consistent with the administration's broader health policy.

As you consider various issues and options in this year's conference, keep in mind that the changes we make in the Civil Service System over the next few years will have far-reaching implications possibly for decades to come. Financial management and human resource management are very important parts of these changes—and it is up to us to assure these changes are in the interest of serving the public in the best manner possible.

Charles A. Bowsher
Comptroller General of the United States

Let me begin by saying that I will keep my remarks brief. First, I agree 100 percent with Connie (Newman) on the issue of having to make some changes and to try to attract the very best people to the government, especially in the financial management field. Many of you may be aware that we have changed our compensation system at the General Accounting Office. I have served this past year, at the request of Congress, on a commission looking at the salary structure for the law enforcement community. I am more convinced that we have to look at our compensation and our personnel systems in the government sector if we are going to compete successfully with the private sector to get the very best people. At the same time, after we get them, we want to train them to be willing to promote the people who are really good workers, and we are anxious to produce great results. We are probably beginning a new era in the personnel area, and I think that Connie and her people who are looking at this area are doing all of us a great favor.

I would also like to congratulate Bill Kendig and all the people from Interior for their very fine efforts and the progress that they are making at that Department. We certainly need that. I think that some of the things that you will hear from Senator John Glenn today are the needs for improved systems, improved audits, and improved financial reports at all the major departments of the federal government. As you may know, I have been strongly recommending that for some time.

I would like to congratulate Ellen O'Connor and the people in the State of Massachusetts who have made great progress in their accounting systems and in their audits. The people from the federal government should recognize that the states have made a lot of progress. We were in Charleston in August when the State of South Carolina got their unqualified opinion on their financial statements for the first time. So there has been a lot of progress made in the state and local governments, and I think we have to match that progress here at the federal level.

It is a great pleasure to see so many people show up for this annual event. I think the program each year has been put together with great care. Looking at the three major topics on the program today--financial statements, systems, and accountability—these are the areas that we have to work on and get them to be first class in all our major departments within the federal government. I would like to congratulate the JFMIP committee that put together the program and put this program on. I look forward to hearing from Senator Glenn on Chief Financial Officer legislation. Thank you very much.

Gerald Murphy
Fiscal Assistant Secretary
Department of the Treasury

Today, it is my great pleasure to present the 1990 Donald L. Scantlebury Memorial Awards for distinguished leadership in financial management improvement to two outstanding leaders in the public sector. The Joint Financial Management Improvement Program named its annual awards to honor and commemorate Donald L. Scantlebury, who made a profound impact on financial management in both the private and public sectors. At the time of his death in June 1981, he was the Chief Accountant and the Director of the Accounting and Financial Management Division of the U.S. General Accounting Office and served on the JFMIP Steering Committee. This award is a continuing tribute to Don, who was a dynamic leader in promoting financial management improvements and a true innovator, always at the forefront of our profession setting high standards for all of us to follow.

This year, we have two award recipients who have demonstrated clearly the broad reaches of the public sector financial management profession. The first awardee is Ellen O'Connor, who is the Budget Director, Fiscal Affairs Division, Executive Office for Administration and Finance, Commonwealth of Massachusetts. During the past 15 years in various leadership positions within the Commonwealth, Ms. O'Connor has been an exceptional role model to her colleagues. In 1985, when she was the Comptroller, she decided to replace the centralized state accounting system, which had been in operation for 17 years. The following year, a completely new centralized accounting system was successfully implemented under her dynamic leadership. The effects of the new system are impressive. Some examples include a decrease of the average turnaround time for vendor payments from 72 day to 28 days and receipt time of financial reports reduced from 2-3 weeks to immediate fiscal information accessibility.

Under Ms. O'Connor's leadership, the Commonwealth of Massachusetts developed and implemented generally accepted accounting principles (GAAP). Massachusetts has produced audited financial statements under both budgetary and GAAP basis of accounting since 1986. This GAAP information is very useful to legislative and executive decision makers.

Another significant accomplishment is the innovative implementation of the State Single Audit. The Federal Single Audit Act of 1984 requires states to complete an audit of all major programs that receive federal funding. The method implemented by Ellen O'Connor in Massachusetts has been to audit the entire Commonwealth as a single entity. This has saved thousands of audit hours and thus hundreds of thousands of dollars in audit fees. In addition, the comprehensive approach yields an effective outcome, since the entire government, and not just portions of it, is evaluated. The efficiency of this approach has been demonstrated in the follow-up and resolution of audit issues, since audit findings that are common and spread across programmatic areas are easily identified for a unified and statewide resolution.

Ms. O'Connor has implemented sound business practices and quality internal control systems to state financial management. For example, she developed new statewide policies and procedures in the area of managing non-tax revenues. With the implementation of these concepts, Massachusetts is now collecting over $60 million in revenues owed that otherwise would have gone uncollected. As Budget Director, she is instituting dramatic changes to the budget development process and the budget execution process. These are only a few of her significant accomplishments, and it is indeed our pleasure to present the 1990 Donald L. Scantlebury Memorial Award to Ellen O'Connor.

The second awardee is Dr. William L. Kendig, Director of Financial Management at the U.S. Department of the Interior. He is being recognized for his dedicated and outstanding leadership in Federal financial management programs, which have resulted in measurable savings involving millions of dollars through cost reductions and systems consolidation activities. One of his first efforts as Director of Financial Management related to the consolidation of five separate payroll systems to one system, which has saved the Department over $1 million per year.

Interior has annual collections ranging from $4 billion to $10 billion, which makes it one of the largest cash collection programs outside the Department of the Treasury. In 1983, he launched a comprehensive departmentwide cash management program to accelerate cash receipts. This program included using a network of lockbox systems, wire transfers, letters of credit, establishing a Diners Club charge card program to minimize travel advances, and promoting the use of payroll direct deposit, thus resulting in savings exceeding $35 million.

One of the greatest and most lasting contributions to federal financial management may be in the area of management controls. Dr. Kendig led an interagency study to review the implementation of the Federal Managers' Financial Integrity Act. The recommendations from this study led to a revision of an OMB circular, a change in audit philosophy, and significantly impacted the way the federal agencies carried out their internal control responsibilities. Thus, his bold leadership led to a revamping in the federal government's approach to this process.

Bill has promoted intergovernmental cooperation and information exchange among financial managers through the founding of the Federal Financial Managers' Council. He also established and chaired the Interagency Internal Control Coordination Council for information exchange on management controls. These are only a few examples of Dr. Kendig's achievements, and we are honored to present the 1990 Donald L. Scantlebury Memorial Award to William L. Kendig.

At the luncheon session (left to right): J. Glenn, R. Willett, L. Gallegos, E. Guss, J.Brown, M. Lujan, G. Murphy, W. Kendig, A. Calhoun, E. O'Connor, D. Fischer, C. Bowsher, C. Newman, F. Hodsoll, D. Chapin, and V. Robinson

Chapter 3
Workshop Summaries

Donald Chapin
General Accounting Office

Financial Statements: Panacea or A Tool?

Donald Chapin, Assistant Comptroller General, General Accounting Office, who moderated this panel, provided an overview on the progress made and problems encountered by federal agencies in preparing audited financial statements. In his opening remarks, he indicated that financial statements were "a bit of both—less than a panacea, but far more than a tool."

Government corporations have been preparing financial statements since 1945. These entities have had years of discipline in the completing of the exercise, developing the supporting systems, and maintaining the accounting skills. This has resulted in organizations that are comfortable in the routine of preparing financial statements. More importantly, organizations have established internal controls structures in systems that can produce reliable financial information.

Federal agencies are relatively new to the financial statement arena. They have found that financial statements are difficult to assemble, and the financial management systems that provide the information to prepare financial statements and to manage the federal resources are often unreliable and incomplete. Agencies must implement fundamental internal controls and have transaction driven double-entry standard general ledger accounting systems, an essential component of any effective financial management system.

Federal agencies need the discipline for preparing reliable financial statements, which satisfy sound and universal standards, in order to focus on fixing the underlying systems. Audited financial statements are report cards which identify seriously deficient systems. Mr. Chapin indicated that fixing these systems would not occur overnight, but could take 2 to 3 years. Subsequent audits by GAO of the same agencies would monitor the improvement effort, provide guidance, and keep the necessary pressure for full correction. GAO will assist in expanding the number of federal agencies preparing financial statements and submitting them for audits. GAO plans to work with federal agencies that receive poor report cards to help them overcome the systems and control problems that cause them to receive low grades.

Mr. Chapin stated that audited financial statements were an integral part of the success of the CFO legislation. The legislation should mandate a certain date by which all major federal agencies must prepare financial statements and have them audited. This action would require agencies to focus high level attention on improving systems and controls so that they can produce reliable financial statements.

Gaylen Larson
Household International

Gaylen Larson, Group Vice President for Household International provided a private sector perspective on financial statements. He stated that business could not succeed in a global economy unless the federal government was a partner. Both the private and public sectors have to be efficient in order to compete. He indicated that financial statements were an instrument of good management control process. If the process was not in place, then a manager could not manage properly assets and liabilities.

Who uses financial statements? In the private sector, it is the investment community, the creditor community, and the management within the corporation. There is application of this same scenario in government. The shareholders in the federal government are the citizens of the country. However, within either structure, it is important not only to summarize the statements at the highest level, but to get them down to middle managers so that the people who are responsible for managing at the product level can manage the full process.

Turning to the preparer community, Mr. Larson stated that there were two important aspects to the total financial management control process:

- Strategic planning requires that all senior and middle managers talk about what they are doing, what they are trying to achieve, who is making the product, can the product be made more efficiently. Thinking of how to do a better job of delivering the goods or services more efficiently and more effectively is critical to a good financial management control system. It establishes the road map for the company for the next 5 years.

- Operating planning is the short cycle planning, normally done over a 12-month period. These plans indicate where "the rubber meets the road." This is where senior managers push down to a departmental level the strategies in the strategic plan; identify how best those strategies can be met; and decide what can be done to eliminate irrelevant costs, become more efficient, and deliver a better product consistent with strategy. If the current product does not support this strategy, then management has to make hard decisions to get rid of unneeded projects or services.

Financial statements must be timely and accurate. He stated that having timely and accurate statements could be done even in the most complex organizations through the development of good financial control systems. A manager can use financial statements as a performance indicator against the organization's operating plan.

Financial statements must have integrity as well as currency. Management cannot let business units camouflage the numbers either by not reporting consistently, switching back and forth from accrual to cash, or otherwise manipulating the data. Ratios are another important area which measure the financial health of an organization. There are strong parallels between the private and public sectors. Both sectors have to be partners to be efficient in order to compete in a global economy.

Anthony McCann
Department of Veteran Affairs

Anthony McCann, Assistant Secretary for Finance and Planning for the Department of Veteran Affairs, provided a dual agency perspective on financial statements. He shared his experiences at the Departments of Health and Human Services and Veteran Affairs. His view was that audited financial statements are extremely important in managing the federal government, but only if the agencies are serious about preparing them. He stated that financial statements allowed the government to put into a common business language the results of their operations. Mr. McCann defined financial statements as one spoke in the "triad of activities in the financial management area" with the other two being the traditional audit function and financial management information.

He raised the following key points:

- How should various accounts be reflected on financial statements? It must be recognized that the federal government does not get money in the same way as the private sector. There need to be different rules to govern this application. For example, a revolving fund account is different from trust fund account or appropriated fund accounts, and different standards must apply.

- When does grant money stop being federal money, and where does federal responsibility stop? What happens when the money is passed down from state to county, city, and then to a nonprofit organization? The recipient may be best able to serve the cause, but it may have not incorporated all the practices of federal financial management.

- What are the economic assumptions that will be used? Who decides which economic assumptions should be used? GAO or OMB?

- Why is the government allowed to use retroactive goal setting? For example, in the 1960s and 1970s, money was given to the public in the form of loan programs that were never expected to be repaid. Congress has changed the rules and the federal government is collecting these debts. There is the need to review the costs and the administration of these programs.

Mr. McCann concluded his remarks by stating that an agency's CFO must be the senior person in that organization and be above the pay line, including the political appointee. If the federal government is not prepared to deal with the issue of how to build financial expertise in the political structure, then the end result will be just paper flow.

Morgan Kinghorn
Office of Management and Budget

Morgan Kinghorn, Director of the Financial Management Division of the Office of Management and Budget, provided a central agency perspective on financial statements and their impact on credit. He stated that "What we got ain't broke. The problem is what we got ain't right either." He indicated that the key to solving this problem was data integrity. The audit of financial statements and other information will authenticate the data integrity. The financial statements can provide a basic anchor to that data which gives it more importance than it has now.

Financial statements are not a panacea and are not the only tool available to managers. The federal government has an enormous amount of tools available, including Financial Integrity Act reports, the Inspector General semi-annual reports, and federal managers reports to audit resolutions. Financial statements are used by a small and special audience, and this audience needs to be expanded.

What is the entity that should prepare financial statements? It may not make sense to do a financial statement for a whole department, such as Health and Human Services, but rather to prepare statements for their bureaus, such as Social Security Administration. Government corporations are essentially business-type organizations that have had audited financial statements. Mr. Kinghorn questioned the rationale of moving on to other agencies unless discipline is imposed on both the financial managers and the program managers.

Financial statements are a fundamental source of fiscal information, and they impose good financial management discipline. The discipline and professionalism that go into financial statements are beneficial in rebuilding financial operations. They define the future agenda.

The basic problem with the financial statements is that in their current form they are fundamentally flawed. There is a need to better define the playing field. The key is that financial statements must be tied closely to budgeting concepts. Managers must focus on budget execution. There must be some way to have these statements focus on the same numbers and the same concepts.

We need to focus attention on where we need to go next. Our attention is focused on those entities that are fundamentally similar to private sector operations. The CFO Council is developing a proposal as part of its financial systems strategy document.

A new series of concepts for federal financial statements must be developed to integrate financial management and budget information. Federal managers need to generate program unit cost information.

Federal managers cannot lose sight of basic concepts and processes that are underway to improve financial management. Financial statements are end products of this entire process. They are an information product. The problem of having a certain statutory date for financial statements with respect to the management decisions is that it is a hazardous process to begin. The statutory timing of financial statements for every department in government would ultimately result in many decisions made that otherwise would not have to be made. Financial statements must be put in government language and until that is done there may be no relevance over the long run.

Managers need to build better technical relationships between budget and finance. We need to develop a broader range of financial statements. Mr. Kinghorn concluded by stating that financial statements are not a panacea, but one tool to be used in government. They need to be put in a common language that makes sense for government.

Alvin Tucker
Department of Defense

Accountability for Government Resources

Alvin Tucker, Deputy Comptroller at the Department of Defense, opened the session by stressing the importance of properly managing and accounting for assets in the federal government. He then introduced the panel members to discuss their experiences concerning accountability issues and the resolution of these issues within their respective organizations.

C. Austin Fitts
Department of Housing and Urban Development

C. Austin Fitts, Assistant Secretary for Housing - Federal Housing Commissioner at the Department of Housing and Urban Development, discussed the initiatives that have been undertaken at her Department to ensure that assets are being accounted for properly at HUD and to get HUD back on a financially sound basis.

First she emphasized that one of the key requisites for accountability is to ensure that managers have the necessary resources and authority required to do their jobs effectively and efficiently. Without resources and authority, managers cannot be held accountable; consequently, top management must be committed in this area. Before managers can be held accountable, they must be provided good financial information with which to manage and control their assets responsibly. When she first came to HUD, she described how program managers were ineffective because they were not being provided good financial information. The managers did not know the status of the resources for which they were responsible.

To rectify the problem, the HUD Secretary announced that the Department would issue independently audited financial statements, both on accrual and cash bases, to managers on a regular and timely basis. Another major action was to have all accounting and financial systems moved from the control of several organizations to the control of a single Federal Housing Administration controller. This consolidation was essential because the program offices reported to one director, while the accounting offices reported to another director, with no communication between the two areas. As a result, the program managers could not be held accountable for the financial impact of their programs since there was no structural integration of the program and financial areas. Ms. Fitts stated that the two changes have been enormously successful at HUD. Financial information will be generated for every HUD program area nationally and regionally so managers will have the proper data to make intelligent decisions.

The newly available financial information has made a revolutionary impact on the making of major policy decision at HUD. She cited examples where program managers intuitively knew that programs were wasteful, but until recently could not be provided with financial information that factually identified these programs for closing.

Ms. Fitts also stressed the importance of providing future as well as historical financial data to managers to enable them to manage a large financial institution such as HUD within the fast moving environment of the 1990s. The Federal Housing Administration is developing econometric modeling capacity to help decision makers develop sensible housing policies for the future and give them the opportunity to look at the operations and address various issues, such as the impact of inflation on future operations.

It is imperative the managers are given historical and future financial information on a frequent basis so they can determine how their operations are doing and make adjustments as necessary. Employees are empowered with information and it is essential that employees have the expertise and automation skills to run programs effectively. She recommended that we must rethink program structure. In many organizations, there are structural impediments to attaining the resources and authority necessary for accountability. We, as managers, must look at structure to see that it helps to provide flexibility and empowerment needed by us and our employees.

Jonathan Kislak
Department of Agriculture

Jonathan Kislak, Deputy Under Secretary of the Small Community and Rural Development at the Department of Agriculture, began by comparing federal managers and private sector managers. He stated that the quality of career and senior staff at his Department is as good or better as any managers he has worked with in the private sector. He believes that given the proper reins, authority and proper tools, federal managers can accomplish anything.

He then discussed his views on some of the differences between the public and private sectors and what can be done together to better manage the financial assets and resources of the federal government. From the perspective of a political appointee, he explained why financial management is difficult to accomplish. First, financial management is viewed as not being glamorous, not understandable, not achievable, not measurable in terms of achievement, and not much fun. It is difficult to set and enforce long-term goals when the average tenure for political appointees is only twenty months and when there is no consensus on the mission of the organizations. For example, there is not always agreement as to whether the Farmers Home Administration is a grant agency or a loan agency. Financial management is made even more difficult because political decisions are frequently given priority over sound management decisions. He cited several examples where political concerns have bearing on the decisions, such as the consolidation of county offices within his Department or the closing of military bases nationwide.

Mr. Kislak then discussed some ways to improve financial management. First, managers must be provided financial information on a timely and regular basis. There is a lack of information, because managers do not ask for it. The key is to provide managers financial information routinely which will force them to use it. A board of directors should be established and reports routinely provided to the board. Team performance measured against goals should be included in the board's agenda. Charts and tables should be provided each month showing trends and activities. In addition, managers should look at current operations and use this information as a tool. For example, an analysis of routine legislative inquiries at his Department identified problems that program managers could then focus on for correction.

Managers should create long-term goals by visualizing operations five years in the future. The financial and program managers must work together on these plans, so that the program managers will understand the financial consequences of their decisions.

Mr. Kislak summarized by stating that financial management can improve by instituting a board of directors, institutionalizing frequent reports, including "sexy" reports that will get managers' attention, establishing milestones, and creating a shared vision for program and financial managers. The toughest part is to get started, but the key is just to get started.

W. E. Douglas
Department of the Treasury

W. E. Douglas, Commissioner of Financial Management Service (FMS) at the Department of the Treasury, discussed his agency's efforts to solve management and accountability problems throughout the federal government. With the increased attention from the Congress, the public, and the press on how the government manages financial resources, we must solve our management control and accountability problems now. We have learned from the savings and loan crisis that solving problems is difficult and complex. We need a new approach to management control that will include the program manager as well as the financial manager. In the 1990s, there is a need to take a more structured, comprehensive and effective approach to identify and solve government financial problems. Both the program and financial manager need a better set of tools to identify weaknesses in management control. We need to act now before there is more waste and embarrassment.

The Financial Management Service is currently undertaking an initiative called "Project USA" to strengthen the management techniques, practices and results of Federal managers in carrying out their financial responsibilities. "USA" stands for a unified systems approach for improving financial management in government. This term "systems" is defined as a comprehensive, consistent and systematic approach to improving both management and accountability for financial consequences of program decisions.

The objectives of Project USA are to (1) identify models of financial management excellence, (2) have models serve as templates to help managers identify strengths and weaknesses of the organization and provide a profile of the agency's effectiveness or ineffectiveness, (3) focus on filling the voids in management controls, (4) ensure that program managers have tools to manage with and use them (i.e. financial systems must provide accurate, timely, accessible, comprehensive and usable information and both program and financial decision makers must use that information to shape their decisions), and (5) hold managers accountable for their financial decisions. Another objective of Project USA is to attract, train, and retain pools of knowledgeable and effective financial managers in the United States.

In January, FMS released a conceptual model of the ideal federal credit system containing key system processes, data elements, and reporting standards necessary to support effective agency credit program management. The pilot single family housing program should be available around the end of March or April. The results will be discussed with the Office of Management and Budget to provide a plan for rolling out the entire Project USA initiative.

In the future, the focus will be on developing financial models for other areas where government has the greatest vulnerability. However, Mr. Douglas stated that Project USA can be fully successful only if OMB and the Congress are willing to use budget dollars and oversight hearings to reward and punish agencies which meet their financial stewardship well or poorly.

He concluded that the bottom line should be for all of us to make major improvements in the management, effectiveness and financial responsibility of Federal programs.

Prescription for System Successes

Jimmie Brown
Office of Management and Budget

Jimmie Brown, Chief of the Financial Systems and Policy Branch, Office of Management and Budget, moderated this session by emphasizing the importance of having solid financial systems throughout the government. He recognized the significance of the Chief Financial Officer legislation that has been proposed by Senator Glenn and the leadership role needed to implement systems successfully. Every major federal agency is conducting an effort toward systems modernization, with a total budget of $600 million. The federal government must have minimum standards and requirements for these systems, and there are ongoing endeavors being conducted by the central agencies. OMB drafted a paper on "A Financial Systems Information Strategy for the Federal Government 1990" that can be used by agencies to upgrade financial systems.

Ray Bell
American Oil Corporation

Ray Bell, Technical Consultant, American Oil Corporation (AMOCO) stated that this corporation has had some system successes and he highlighted what AMOCO has learned. One important point is that you can not do all things you read about, and you shouldn't try to do them all. To implement a system successfully, you should pick one driving force and let that guide your systems decisions. Client satisfaction is AMOCO's driving force for system success. When the client is pleased with the results produced by the system, then the system is a success. Three ingredients that contribute to client satisfaction and system success are:

1. Functionality - what the system does. This is the primary ingredient for system success, and this must be clearly defined with ideas, such as

- partnership - systems developers and clients should jointly pursue technological business solutions - and
- detailed requirements - mutually-agreed business needs are to be clear and well understood (the techniques that AMOCO used to gather these requirements were joint application design, prototyping, and pilots).

2. Environmental fit - how the system fits in. This is an integral piece of the total systems area, which is composed of

- architecture - a set of rules and structure for defining an environment.
- standards - they are necessary for systems success and examples would be architecture components. The most important standard is methodology, and there needs to be a systems development methodology used throughout the organization that makes sense.
- technology management - you need to investigate new technology and phase out the old.

3. Efficiency - how the system runs. The emphasis today is to get the system implemented quickly and to reduce maintenance requirements. You will have to weigh the benefits (functionality) and cost (efficiency). Four key ingredients that make up efficiency are:

- reusable code - this is a significant factor in productivity or efficiency;
- purchased projects - purchase rather than build;
- project size - this will affect efficiency in the way that large projects have a high probability of failure and small projects have too much overhead; and
- re-engineering - this deals primarily with updating technology and structured code.

Timothy Bowling
General Accounting Office

Tim Bowling, Assistant Director, Information Management and Technology Division, General Accounting Office, stated that GAO conducted a symposium to explore ways of successfully integrating information technology into the business of government, and he briefly described the results. Leaders from industry, Congress and the Executive Branch were brought together to focus on successful examples that industry implemented that solved problems similar to the government. The symposium established a high-level dialogue among key participants in the information technology field and provided a framework of principles for organizations to use in integrating information technology into their business. The five principles are

1. Commitment and vision at the top - The leader must play a central role in providing a vision of how the organization will operate in the future. This vision must bond together information technology with the business of the organization. This bonding is an essential element in the process. It is important that the vision be a clear guiding statement that can be understood by all and can be used to inform business decisions and technology decisions.

2. Alliances and partnerships - There are three levels:

- external alliances - Other agencies, private industry, or advisory groups are encouraged to share perspectives and learn from each other's experiences.
- internal partnerships - Between program offices and technical groups, partnerships should be fostered to ensure that technology is integrated with the business of the organization.

3. Congress and the oversight agencies - The organization should do everything it can to ensure that Congress understands and buys into the overall direction the organization is taking.

- Service to the public - The basis for all business and technology decisions should be the users. In assessing their needs, you should not rely on their demands of the past, but make a thorough assessment of the users' needs.

4. Embody the vision in a clear yet flexible systems architecture - This will serve as a blueprint, an umbrella for all individual systems within the organization. The architecture should specify functions and relationships between functions. This approach should eliminate incompatible and duplicative systems and make integration easier. A modular approach to building the system is safer and returns benefits of the system faster. It can also respond to changes in direction or advances in technology.

5. Management continuity is needed - Many organizations change managers frequently which obscures accountability for the system's success and often leads to changes in direction. If this is the case, we need to make sure that the organization's long-term strategy is clearly articulated to help ensure more consistent direction; and advisory groups should be established to help provide continuity.

In closing, Mr. Bowling observed that committed and visionary leadership is the foundation for all of these principles. The framework is designed from a top-down perspective that depends on top management's ability to envision the future and its commitment to making that vision a reality.

Gerald Riso
Riso and Dempsey

Gerald Riso, Senior Partner, Riso and Dempsey, described his ideas for system success. He agreed that top management involvement is required and that there is a need for continuity in implementing systems successfully. Too much of systems work is frozen in time; systems developers and users should be more flexible in implementing systems. The direct involvement by program people is required. His recommendations for systems successes include

- assurance of adequate resources to follow through on all phases of the system project,
- scheduled reassurances,
- strong project management leadership,
- competent staff in all phases of the project (assures that the system is fully tested and implemented),
- economic justification,
- efficiency (benefits exceed the costs of developing and maintaining the system), and
- luck.

He addressed the need for more incentives for performance. In closing, Mr. Riso stated that it is the best interest of all parties concerned that the government should increase its efforts to improve financial systems and to place more emphasis on cash and credit management.

Chapter 4
Award Winners

Donald L. Scantlebury Memorial Award Winners

1989

William L. Kendig
Director of Financial Management
Department of the Interior

Ellen O'Connor
Budget Director,
Fiscal Affairs Division,
Executive Office for
Administration and Finance
Commonwealth of Massachusetts

1988

Kenneth P. Boehne
Chief Executive Officer
U.S. Railroad Retirement Board

Louis L. Goldstein
Comptroller of the Treasury
State of Maryland

Elizabeth E. Smedley
Deputy Assistant Secretary for
Financial Management and Controller
Department of Energy

1987

Conrad R. Hoffman
Director,
Office of Budget & Finance
(Controller)
Veterans Administration

William R. Snodgrass
Comptroller of the Treasury
State of Tennessee

1986

William R. Douglas
Commissioner, Financial
Management Service
Department of the Treasury

Douglas R. Norton
Auditor General
State of Arizona

John R. Quetsch
Principal Deputy Asst. Secretary
(Comptroller)
Department of Defense

1985

C. Morgan Kinghorn
Comptroller
Environmental Protection Agency

Edward J. Mazur
State Comptroller
State of Virginia

1984

Clyde E. Jeffcoat
Deputy Commissioner
Department of the Army

Earle E. Morris
Comptroller General
State of South Carolina

1983

Roger B. Feldman
Comptroller
Department of State

James F. Antonio
State Auditor
State of Missouri

1982

Harold L. Stugart
Auditor General
Department of the Army

Roland W. Burris
Comptroller
State of Illinois

1981

David Sitrin
Deputy Associate Director for National Security
Office of Management & Budget

Thomas W. Hayes
Auditor General
State of California

Financial Management Improvement Award Winners

1980

Marcus Page
Director, Division of Financial Management
Environmental Protection Agency

Ronald Cronson
Auditor General
State of Illinois

1979

June Gibbs Brown
Inspector General
Department of the Interior

Anthony Piccirilli
Auditor General
State of Rhode Island

1978

William M. Henderson
Fiscal Affairs Specialist
Department of the Treasury

Frank L. Greathouse
Director, Division of Department of the Treasury
State and Municipal Audit
State of Tennessee

1977

Rear Admiral James R. Ahern
Deputy Comptroller of the Army
Department of the Army

Lloyd F. Hara
Auditor, King County
State of Washington

1976

Alice M. Rivlin
Director
Congressional Budget Office

Joseph T. Davis
Assistant Commissioner (Administration)
Internal Revenue Service

1975

Terrence E. McClary
Assistant Secretary of Defense (Comptroller)
Department of Defense

John E. Dever
City Manager of Sunnyvale
State of California

1974

Bernard B. Lynn
Director
Defense Contract Audit Agency

Martin Ives
Deputy Comptroller
State of New York

1973

Edward S. Stepnick
Director, HEW Audit Agency
Department of Health, Education and Welfare

Robert R. Ringwood
State Auditor
State of Wisconsin

1972

Robert C. Moot
Assistant Secretary of Defense (Comptroller)
Department of Defense

Richard W. Miller
Associate Asst. Secretary for Administration
Department of Labor

1971

J. Patrick Dugan
Treasurer-Controller
Export-Import Bank

John P. Abbadessa
Controller
Atomic Energy Commission

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