

June 2012

MANAGEMENT REPORT

Improvements Needed in Controls over the Preparation of the U.S. Consolidated Financial Statements



G A O

Accountability * Integrity * Reliability



Highlights of [GAO-12-529](#), a report to agency officials

Why GAO Did This Study

Treasury, in coordination with OMB, is primarily responsible for preparing the *Financial Report*, which contains the CFS. Since GAO's first audit of the fiscal year 1997 CFS, certain material weaknesses and other limitations on the scope of GAO's work have prevented GAO from expressing an opinion on the CFS, exclusive of the Statement of Social Insurance (SOSI). Also, GAO was unable to express opinions on the 2011 and 2010 SOSI and the 2011 Statement of Changes in Social Insurance Amounts because of significant uncertainties, primarily related to the achievement of projected reductions in Medicare cost growth, reflected in these statements.

As part of the fiscal year 2011 CFS audit, GAO identified material weaknesses and other control deficiencies in the processes used to prepare the CFS. The purpose of this report is to (1) provide details on new control deficiencies GAO identified related to the preparation of the CFS, (2) recommend improvements, and (3) provide the status of corrective actions taken to address GAO's prior recommendations in this area that remained open at the end of the fiscal year 2010 audit.

What GAO Recommends

GAO is making 10 recommendations—9 to Treasury and 1 to OMB—to address new control deficiencies. In commenting on GAO's draft report, Treasury and OMB generally concurred with GAO's findings.

View [GAO-12-529](#). For more information, contact Gary Engel at (202) 512-3406 or engelg@gao.gov.

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MANAGEMENT REPORT

Improvements Needed in Controls over the Preparation of the U.S. Consolidated Financial Statements

What GAO Found

During its audit of the fiscal year 2011 consolidated financial statements of the U.S. government (CFS), GAO identified new and continuing control deficiencies in the Department of the Treasury's (Treasury) and the Office of Management and Budget's (OMB) processes used to prepare the CFS. These control deficiencies contributed to material weaknesses in internal control over the federal government's ability to

- adequately account for and reconcile intragovernmental activity and balances between federal entities;
- ensure that the federal government's accrual-based consolidated financial statements were consistent with the underlying audited entities' financial statements, properly balanced, and in conformity with U.S. generally accepted accounting principles; and
- identify and either resolve or explain material differences between (1) components of the budget deficit that are used to prepare certain information in the CFS and (2) related amounts reported in federal entities' financial statements and underlying financial information and records.

GAO identified new control deficiencies involving the need to

- develop or revise and implement written procedures for appropriate Treasury and OMB officials to (1) review and approve the drafts of the *Financial Report of the United States Government (Financial Report)* before they are provided to GAO and (2) better ensure that key federal entity personnel are actively involved in the process for preparing and reviewing the *Financial Report*;
- enhance procedures for timely review, approval, and use of the CFS disclosure checklist;
- develop procedures for pursuing indications that financial information provided by federal entities for inclusion in the CFS may not be in conformity with applicable accounting standards;
- enhance Treasury's intragovernmental data validation process; and
- enhance procedures for timely identifying, notifying, and obtaining closing packages from federal entities as they first become significant to the *Financial Report*.

In addition, GAO found that various other control deficiencies identified in previous years' audits with respect to the CFS preparation continued to exist. Specifically, of the 50 open recommendations from GAO's prior reports regarding control deficiencies in the CFS preparation process, 12 were closed and 38 remained open as of December 12, 2011, the date of GAO's report on its audit of the fiscal year 2011 CFS. GAO will continue to monitor the status of corrective actions taken to address the 10 new recommendations as well as the 38 open recommendations from prior years as part of its fiscal year 2012 CFS audit.

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Abbreviations

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|-------------------------|---|
| AGA | Association of Government Accountants |
| CFO | chief financial officer |
| CFS | consolidated financial statements of the U.S. government |
| FASAB | Federal Accounting Standards Advisory Board |
| FEVBP | Federal Employee and Veteran Benefits Payable |
| <i>Financial Report</i> | <i>Financial Report of the United States Government</i> |
| FMS | Financial Management Service |
| FRD | Financial Reports Division |
| GAAP | generally accepted accounting principles |
| GFRS | Governmentwide Financial Report System |
| IRAS | Intragovernmental Reporting and Analysis System |
| Justice | Department of Justice |
| MD&A | Management's Discussion and Analysis |
| OFAS | Office of the Fiscal Assistant Secretary |
| OMB | Office of Management and Budget |
| SFFAS | Statement of Federal Financial Accounting Standards |
| SOP | standard operating procedure |
| SOSI | Statement of Social Insurance |
| STAR/CARS | Treasury's central accounting and reporting system |
| Treasury | Department of the Treasury |
| TVA | Tennessee Valley Authority |

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G A O

Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

June 27, 2012

The Honorable Timothy F. Geithner
Secretary of the Treasury

The Honorable Jeffrey Zients
Acting Director
Office of Management and Budget

In our report dated December 12, 2011,¹ we disclaimed an opinion on the consolidated financial statements of the U.S. government (CFS) for the fiscal years ended September 30, 2011 and 2010,² except for the 2009, 2008, and 2007 Statements of Social Insurance (SOSI), which received unqualified opinions.³ Since GAO's first audit of the fiscal year 1997 CFS, certain material weaknesses in internal control over financial reporting and other limitations on the scope of our work have resulted in conditions that prevented us from expressing an opinion on the federal government's accrual-based consolidated financial statements.⁴ These include material weaknesses that relate to the federal government's processes used to prepare the CFS. Such material weaknesses involve the federal government's inability to

¹The 2011 *Financial Report of the United States Government* includes our report and was issued by the Department of the Treasury on December 23, 2011, and is available through GAO's website at <http://www.gao.gov/financial.html> and Treasury's website at <http://www.fms.treas.gov/fr/index.html>.

²The CFS for the fiscal years ended September 30, 2011 and 2010, consist of the Statements of Net Cost, Statements of Operations and Changes in Net Position, Reconciliations of Net Operating Cost and Unified Budget Deficit, Statements of Changes in Cash Balance from Unified Budget and Other Activities, Balance Sheets, the 2011, 2010, 2009, 2008, and 2007 Statements of Social Insurance, and the 2011 Statement of Changes in Social Insurance Amounts, including the related notes to these financial statements.

³Because of significant uncertainties (discussed in Note 26 to the consolidated financial statements), primarily related to the achievement of projected reductions in Medicare cost growth reflected in the 2011 and 2010 SOSI, we were unable to, and did not, express opinions on the 2011 and 2010 SOSI as well as on the 2011 Statement of Changes in Social Insurance Amounts. We were, however, able to render unqualified opinions on the 2009, 2008, and 2007 SOSI.

⁴As used in this report, accrual-based consolidated financial statements refer to all of the consolidated financial statements and notes, except for those related to the SOSI and the Statement of Changes in Social Insurance Amounts.

-
- adequately account for and reconcile intragovernmental activity and balances between federal entities;
 - ensure that the federal government's accrual-based consolidated financial statements were consistent with the underlying audited entities' financial statements, properly balanced, and in conformity with U.S. generally accepted accounting principles; and
 - identify and either resolve or explain material differences between (1) certain components of the budget deficit reported in the Department of the Treasury's (Treasury) central accounting records that are used to prepare the Reconciliation of Net Operating Cost and Unified Budget Deficit, the Statement of Changes in Cash Balance from Unified Budget and Other Activities, and the Fiscal Projections for the U.S. Government (included in Supplemental Information) and (2) related amounts reported in federal entities' financial statements and underlying financial information and records.

Treasury, in coordination with the Office of Management and Budget (OMB), prepares the CFS on behalf of the federal government.⁵ Several of the material weaknesses⁶ in internal control over financial reporting that have contributed to our continuing disclaimers of opinion on the federal government's accrual-based consolidated financial statements were identified by other auditors during their audits of individual federal entities' financial statements and were reported in detail with recommendations to the entities in separate reports.

The purpose of this report is to provide (1) detailed information on new control deficiencies identified during our fiscal year 2011 audit that relate to the processes used to prepare the CFS, (2) 10 recommendations to address these new control deficiencies, and (3) the status of corrective actions taken by Treasury and OMB to address the 50 recommendations relating to the processes used to prepare the CFS detailed in our previous reports that remained open at the end of the fiscal year 2010

⁵The Government Management Reform Act of 1994 has required such reporting, covering the executive branch of government, beginning with financial statements prepared for fiscal year 1997. 31 U.S.C. 331(e).

⁶A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.

audit. We closed 12 of the 50 recommendations at the end of the fiscal year 2011 audit. We closed 4 of these recommendations based on Treasury's progress to date and opened new recommendations that are better aligned with the current status of the remaining internal control deficiencies related to these areas. Appendix I provides a summary of the status of actions taken to address the open recommendations from our previous reports as of December 12, 2011, the date of our report on the audit of the fiscal year 2011 CFS.

Scope and Methodology

As part of our audit of the fiscal years 2011 and 2010 CFS, we considered the federal government's financial reporting procedures and related internal control. Also, we determined the status of corrective actions taken by Treasury and OMB to address open recommendations relating to the processes used to prepare the CFS detailed in our previous reports. Based on the scope of our work and the effects of the other limitations on the scope of our audit noted throughout our audit report on the fiscal year 2011 CFS, our internal control work would not necessarily identify all deficiencies in internal control, including those that might be material weaknesses or significant deficiencies.⁷ We have communicated each of the new control deficiencies to your staff. We performed our audit of the fiscal years 2011 and 2010 CFS in accordance with U.S. generally accepted government auditing standards. We believe that our audit provided a reasonable basis for our conclusions in this report.

We requested comments on a draft of this report from the Acting Director of OMB and the Secretary of the Treasury or their designees. OMB provided oral comments, which are summarized in the Agency Comments section of this report. Treasury's Fiscal Assistant Secretary provided written comments on June 7, 2012, which are reprinted in their entirety in appendix II and are also summarized in the Agency Comments section.

⁷A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Review and Approval of the *Financial Report*

Over the past several years, Treasury and OMB have improved the process for preparing the *Financial Report of the United States Government (Financial Report)*⁸ and have addressed several of the issues underlying prior years' recommendations, including our recommendation regarding the preparation and review of the Management's Discussion and Analysis and Citizen's Guide sections of the *Financial Report*. However, we continued to identify numerous incorrect amounts and inconsistent and incomplete disclosures in the draft 2011 *Financial Report*, including the consolidated financial statements, and the Notes and Supplemental Information sections of the *Financial Report*. These errors, inconsistencies, and omissions occurred more frequently in the relatively new and in more complex areas of the *Financial Report*. For example, several note disclosures in the draft *Financial Report* related to social insurance, the Troubled Asset Relief Program, Government-Sponsored Enterprises, and federal employee and veteran benefits were inconsistent with related disclosures in federal agencies' Performance and Accountability Reports or Agency Financial Reports, and in some cases were not accurate or complete. The errors, inconsistencies, and omissions were not identified through Treasury's and OMB's processes for preparing and reviewing the draft *Financial Report*. We communicated these matters to Treasury and OMB officials who revised the *Financial Report*, as appropriate.

While Treasury maintains standard operating procedures for preparing, reviewing, and approving the *Financial Report*, the extent of errors, inconsistencies, and omissions we identified is evidence of deficiencies in Treasury's process for preparing and reviewing the draft *Financial Report*, particularly with respect to relatively new areas and in more complex areas. Treasury procedures did not provide for key federal entity personnel with technical expertise in the relatively new and the more complex areas to be actively involved in the preparation and review process of the *Financial Report*. More active involvement of such key federal entity personnel can help prevent or detect and correct incorrect

⁸The *Financial Report* comprises the consolidated financial statements, related notes, stewardship information, supplemental information, and other accompanying information, including the Citizen's Guide and Management's Discussion and Analysis. The Citizen's Guide presents information regarding the financial position and condition of the U.S. government and discusses key financial topics. The Management's Discussion and Analysis assists in (1) communicating management's insights about the reporting entity, (2) increasing the understandability and usefulness of the financial report, and (3) providing information about the reporting entity and its operations and challenges.

amounts and inconsistent and incomplete disclosures. Further, Treasury's procedures for preparing and reviewing the *Financial Report* did not require review and approval of drafts of the *Financial Report* by appropriate higher-level Treasury officials of the Office of the Fiscal Assistant Secretary before they were provided to GAO for audit.⁹ Also, although OMB had certain informal procedures for its Office of Federal Financial Management's review and approval of drafts of the *Financial Report* before they were provided to GAO, it had not documented these procedures. Documented procedures that clearly delineate the roles and responsibilities of the appropriate Treasury and OMB officials can help to provide an effective review process.

According to *Standards for Internal Control in the Federal Government*, one of the key objectives of an organization's internal control over financial reporting is to provide reasonable assurance as to the reliability of its financial reporting, including its financial statements.¹⁰ Without effectively implemented preparation, review, and approval processes for drafts of the *Financial Report*, Treasury and OMB are at risk of presenting information that is incorrect, inconsistent, or incomplete.

Recommendations for Executive Action

We recommend that the Acting Director of OMB direct the Controller of OMB to develop and implement written procedures specifying the steps required for effectively reviewing and approving the drafts of the *Financial Report* before they are provided to GAO, to include clear delineation of the review and approval roles and responsibilities of designated appropriate higher-level officials in OMB's Office of Federal Financial Management, including the Controller of OMB.

We also recommend that the Secretary of the Treasury direct the Fiscal Assistant Secretary to revise and implement Treasury's procedures

⁹The Secretary of the Treasury, in coordination with the Director of OMB, is required to annually submit financial statements of the U.S. government to the President and the Congress. The Office of the Fiscal Assistant Secretary and the Office of Federal Financial Management are the respective offices within Treasury and OMB that have primary responsibility for performing this function.

¹⁰GAO, *Standards for Internal Control in the Federal Government*, [GAO/AIMD-00-21.3.1](#) (Washington, D.C.: November 1999). These standards define the minimum level of quality acceptable for internal control in the government and provide the basis against which internal control is to be evaluated.

related to preparing and reviewing the drafts of the *Financial Report* before they are provided to GAO, to include clear delineation of the review and approval roles and responsibilities of designated appropriate higher-level officials in the Office of the Fiscal Assistant Secretary, including the Fiscal Assistant Secretary.

We further recommend that the Secretary of the Treasury direct the Fiscal Assistant Secretary, working in coordination with the Controller of OMB, to develop and implement procedures to provide for the active involvement of key federal entity personnel with technical expertise in relatively new areas and more complex areas in the preparation and review process of the *Financial Report*.

Timely Review and Approval of the Financial Reporting Disclosure Checklist

For many years, we have reported that Treasury had not established a formal process to reasonably assure that the CFS, including the related notes, were presented in conformity with generally accepted accounting principles (GAAP).¹¹ Over the past several years, Treasury has developed procedures utilizing a financial reporting disclosure checklist (CFS disclosure checklist) that is intended to significantly improve Treasury's ability to timely identify GAAP requirements, assess the effect of any omitted disclosures, and document decisions reached with regard to the omission of any disclosures and the rationale for such decisions. However, during our audit of the fiscal year 2011 CFS, we determined that Treasury's assessment and documentation regarding the reporting of certain financial information required by GAAP continued to be impaired. Specifically, we found that Treasury officials did not complete and document their required review and approval of the CFS disclosure checklist within the time frames established by Treasury's policies and procedures.

In response to our prior recommendation, Treasury developed procedures, including use of its CFS disclosure checklist, to help determine that all disclosures required by GAAP are included in the CFS. Several years ago, Treasury established a standard operating procedure (SOP), entitled "The FR Disclosure List," to update the CFS disclosure checklist to reflect new disclosures that are required to be included in the

¹¹The Federal Accounting Standards Advisory Board is the body designated by the American Institute of Certified Public Accountants as the source of generally accepted accounting principles for federal reporting entities.

CFS. In fiscal year 2011, Treasury further enhanced the SOP to include procedures for periodically updating the CFS disclosure checklist and documenting preparer sign-offs and managerial approvals. Specifically, the fiscal year 2011 enhancement to the SOP requires the CFS disclosure checklist to be revised annually, as necessary, to incorporate any (1) new and amended disclosure requirements effective for the current year's reporting and (2) additional information necessary to address GAO audit recommendations related to financial disclosure. The SOP was also modified to require a final review and sign-off on the CFS disclosure checklist by the Financial Reports Division (FRD) Director in Treasury's Financial Management Service (FMS) by December 5, 2011, to help provide reasonable assurance that the disclosures are in conformity with GAAP.¹² However, we found that the final review and approval by the FRD Director was not completed and documented by December 5, 2011, as required by the SOP. We also noted that the SOP did not require Treasury to use the CFS disclosure checklist to assist in preparing the format draft that Treasury prepares in advance of the year-end consolidation. Using the CFS disclosure checklist to assist in preparing the format draft could assist Treasury in completing the final checklist on a timely basis.

As a result, Treasury was limited in its ability to rely on the CFS disclosure checklist to reasonably assure that the CFS was prepared in conformity with GAAP as intended by the SOP. Specifically, the lack of timely review and approval of the CFS disclosure checklist limited Treasury's ability to reasonably assure that all GAAP-required disclosures are included in the CFS.

Recommendations for Executive Action

To help to provide reasonable assurance that the information reported in the CFS is complete, accurate, and in conformity with GAAP, the Secretary of the Treasury should direct the Fiscal Assistant Secretary to (1) establish a mechanism to ensure that Treasury's CFS disclosure checklist is reviewed and approved by the date in Treasury's policies and procedures and (2) revise the SOP to include requirements for using the CFS disclosure checklist to prepare the format draft of the CFS and to

¹²Treasury's SOP is modified annually to include new due dates for updating the CFS disclosure checklist to correspond with the current fiscal year CFS reporting requirements. In fiscal year 2011, Treasury required the CFS disclosure checklist to be reviewed and approved by December 5, 2011.

update the CFS disclosure checklist as necessary when subsequent drafts of the CFS are prepared.

Review of Federal Entities' Financial Information for Inclusion in the CFS

Over the past several years, Treasury has made progress in developing, documenting, and implementing numerous improvements to its SOPs intended to enhance internal control over the process for preparing the CFS. However, in fiscal year 2011, we identified a control deficiency involving Treasury's review of audited closing packages.¹³ In connection with Treasury's role as preparer of the CFS, Treasury management is responsible for developing and documenting detailed policies and procedures for preparing the CFS and ensuring that appropriate internal control is built into and is an integral part of the CFS compilation process. *Standards for Internal Control in the Federal Government* calls for clear documentation of policies and procedures.

Treasury's SOP entitled "Data Analysis" includes procedures for Treasury staff to compare financial information submitted by federal entities through their audited closing packages to the entities' audited financial statements for consistency and to work with the entities to correct any material inconsistencies identified by Treasury. However, Treasury's SOP did not include steps to pursue instances where the information provided to Treasury contains indications that federal entities' financial information submitted through the closing package, even if consistent with the entities' audited financial statements, may not be in conformity with GAAP. Steps to pursue these instances would be particularly relevant when a new federal accounting standard is implemented to reasonably assure appropriate and consistent application across government. For example, as part of its fiscal year 2011 CFS compilation process, Treasury did not identify federal entities' potential GAAP exceptions related to Statement of Federal Financial Accounting Standards No. 33, *Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, which was first implemented in fiscal year 2010. As part of our fiscal year 2011 audit, we

¹³The closing package methodology links federal entities' audited consolidated department-level financial statements to the CFS. Verifying entities' chief financial officers must verify the consistency of the closing package data with these entities' audited financial statements. In addition, for most verifying entities, the full closing package is required to be audited.

raised concerns that the financial information presented at the governmentwide level, which was provided by federal entities, may not be in conformity with GAAP. However, there was not sufficient time for Treasury to pursue and resolve our concerns. As a result, Treasury was unable to reasonably assure that such Federal Employee and Veteran Benefits Payable information in the fiscal year 2011 CFS was presented in conformity with GAAP. Inadequate policies and procedures increase the risk that errors in the compilation process could go undetected and result in misstatements in the financial statements or incomplete and inaccurate disclosure of information within the *Financial Report*.

Recommendation for Executive Action

To help to provide reasonable assurance that financial information is properly reported in the CFS, we recommend that the Secretary of the Treasury direct the Fiscal Assistant Secretary to enhance the SOP entitled “Data Analysis” to include required steps for pursuing any instances where the information provided to Treasury contains indications that financial information provided by federal entities for inclusion in the CFS may not be in conformity with GAAP, particularly with respect to any recent changes in GAAP.

Treasury’s Intragovernmental Data Validation Process

The *Treasury Financial Manual* section entitled “Agency Reporting Requirements for the Financial Report of the United States Government” requires federal entities to report intragovernmental balances quarterly to Treasury and work with their trading partners to reconcile and resolve intragovernmental differences. Treasury developed the Intragovernmental Reporting and Analysis System (IRAS) to begin to address the long-standing weakness we reported regarding the federal government’s inability to adequately account for and reconcile intragovernmental activity and balances. Using IRAS, Treasury generates reports on a quarterly basis to assist federal entities in identifying, reconciling, and resolving intragovernmental differences with their trading partners prior to year-end reporting. Further, Treasury personnel use IRAS reports to monitor entities’ progress in reconciling their intragovernmental differences both quarterly and at year-end. Treasury’s SOP entitled “Intragovernmental Quarterly Reporting Process and Analysis” includes IRAS validation procedures for Treasury personnel to validate the IRAS reports for accuracy prior to providing them to federal entities. However, during our fiscal year 2011 audit, we found control deficiencies over the design and implementation of the IRAS data validation process.

Specifically, during our fiscal year 2011 audit, we found that one individual at Treasury, who was the developer of IRAS, also had several other incompatible roles and responsibilities, including serving as the IRAS administrator as well as a review accountant for one of the federal entities included in the IRAS process. In these various roles, his responsibilities included uploading the federal entities' reported intragovernmental data into IRAS, using IRAS to process the data and generate the IRAS reports, and monitoring his assigned entity's progress in reconciling and resolving the intragovernmental differences with its trading partners. As such, his roles included responsibilities for much of the process for identifying, reconciling, and resolving intragovernmental differences.

Standards for Internal Control in the Federal Government calls for segregation of duties among different people in order to reduce the risk of error or fraud, thus preventing a single individual from having full control of a transaction or event. Treasury noted that it reduced the risk of error through the required quarterly IRAS validation process, which provides for the IRAS administrator to verify randomly selected federal entities' submitted data for consistency and completeness with IRAS reports. The process also calls for the IRAS team leader to review and approve the IRAS administrator's testing documentation prior to the distribution of IRAS reports to the federal entities. In addition, the process includes completing a checklist to document that these procedures have been performed. If properly designed and effectively implemented, this process could reduce the risk of error caused by inadequate segregation of duties. However, we found that although the IRAS validation process calls for testing of randomly selected federal entities' data with IRAS reports for consistency and completeness, this procedure did not require testing of the federal entity that the administrator was responsible for under his review accountant's role. Further, we found that since the IRAS validation checklist has been in place—the third and fourth quarters of fiscal year 2011—the completed checklists did not always include the IRAS team leader's signature to document that the required review took place. We also noted that the data from IRAS were provided to federal entities for use prior to the validations, increasing the risk of entities receiving inaccurate reports.

These deficiencies in the design and implementation of the IRAS validation process impair Treasury's assurance that it has reduced the risk of error in the IRAS reports that Treasury and federal entities depend on to help identify and reconcile intragovernmental differences between federal entities and their trading partners.

Recommendations for Executive Action

To help to provide reasonable assurance that appropriate controls are in place to reduce the risk of errors in IRAS reports, we recommend that the Secretary of the Treasury direct the Fiscal Assistant Secretary to (1) enhance the IRAS validation procedures, at a minimum, to include specific steps for testing intragovernmental data of the administrator's assigned entity and (2) establish a mechanism for ensuring that all steps in the required validation process are completed, documented, and reviewed prior to the distribution of IRAS reports.

Timely Submission of Audited Closing Packages by Newly Identified Significant Federal Entities

Treasury's SOP entitled "Significant Federal Entities Identification" includes procedures for Treasury to annually¹⁴ assess whether federal entities that were previously determined nonsignificant, have become significant to the *Financial Report*. The SOP also includes procedures for Treasury, in coordination with OMB, to help provide reasonable assurance that any newly identified significant entities comply with the reporting requirements for significant entities. Treasury's assessments are based on prior year financial information. In addition, the SOP requires federal entities identified as significant to the *Financial Report* to submit a closing package to Treasury that includes audited special purpose financial statements that have been appropriately reclassified in accordance with CFS reporting requirements for inclusion in the *Financial Report*.

In fiscal year 2011, we found that Treasury's and OMB's processes were not effective in ensuring timely submission of audited closing packages by entities newly identified as significant to the *Financial Report* because of deficiencies in the design of Treasury's related policies and procedures. Specifically, we found that Treasury's SOP did not include procedures to (1) identify any federal entities that became significant to the *Financial Report* during the fiscal year but were not identified as significant in the prior fiscal year and (2) obtain audited closing packages from newly identified entities in the year they are determined to be significant, including timely written notification to newly identified significant entities. Without these procedures, Treasury is unable to reasonably assure that it has appropriate audit assurance over financial information for all federal entities that are significant to the *Financial Report*.

¹⁴Prior to fiscal year 2011, Treasury's SOP called for biennial assessments for entities with a fiscal year end and for triennial assessments for entities with a calendar year end. In fiscal year 2011, Treasury revised this SOP to require annual assessments.

Recommendations for Executive Action

To help to provide reasonable assurance that Treasury timely receives the audited closing package from those federal entities that are newly identified as being significant to the *Financial Report*, we recommend that the Secretary of the Treasury direct the Fiscal Assistant Secretary, working in coordination with the Controller of OMB, to enhance the SOP entitled “Significant Federal Entities Identification” to include procedures for (1) identifying any entities that become significant to the *Financial Report* during the fiscal year but were not identified as significant in the prior fiscal year and (2) obtaining audited closing packages from newly identified significant entities in the year they become significant, including timely written notification to newly identified significant entities.

Status of Recommendations from Prior Reports

Of our 50 recommendations from our prior reports regarding control deficiencies in the CFS preparation process that were open at the end of the fiscal year 2010 audit, we were able to close 12 during our fiscal year 2011 audit, generally as a result of corrective actions taken by Treasury. The other 38 recommendations remained open as of December 12, 2011, the date of our report on the audit of the fiscal year 2011 CFS.

Appendix I summarizes the status as of December 12, 2011, for the 50 open recommendations from our prior years’ reports. Specifically, appendix I includes the status according to Treasury and OMB, as well as our own assessments where appropriate. The status of recommendations per GAO includes explanatory comments on Treasury’s and OMB’s information. We will continue to monitor Treasury’s and OMB’s progress in addressing our recommendations as part of our fiscal year 2012 CFS audit.

Agency Comments

OMB Comments

In oral comments on a draft of this report, OMB generally concurred with the findings in this report.

Treasury Comments

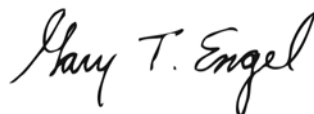
In written comments on a draft of this report, Treasury concurred with our findings and noted that the agency has made significant progress in enhancing its policies and procedures for the CFS preparation since the issuance of the fiscal year 2011 audit report. Also, Treasury stated that it expects to implement additional recommendations by the end of fiscal year 2012, and that it will use our findings to continue to improve the

central accounting and compilation activities associated with the CFS. In addition, Treasury stated that it has given great management attention and staff resources to resolving material intragovernmental differences along with developing or improving process controls within FMS and the federal agencies. Treasury also stated that its strategy includes the use of multiple focus groups that have identified both short- and long-term solutions through analysis of material differences and working closely with agencies to identify root causes of differences. Further, Treasury stated that it has developed General Fund accounts that will provide Treasury with the capability to reconcile to federal agency financial reporting data.

This report contains recommendations to you. The head of a federal agency is required by 31 U.S.C. 720 to submit a written statement on actions taken on our recommendations to the Senate Committee on Homeland Security and Governmental Affairs and to the House Committee on Oversight and Government Reform not later than 60 days after the date of this report. A written statement must also be sent to the Senate and House Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of this report.

We are sending copies of this report to interested congressional committees, the Fiscal Assistant Secretary of the Treasury, and the Controller of OMB's Office of Federal Financial Management. In addition, this report is available at no charge on the GAO website at <http://www.gao.gov>.

We acknowledge and appreciate the cooperation and assistance provided by Treasury and OMB during our audit. If you or your staff have any questions or wish to discuss this report, please contact me at (202) 512-3406 or engelg@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report.



Gary T. Engel
Director
Financial Management and Assurance

Appendix I: Status of Treasury's and OMB's Progress in Addressing GAO's Prior Year Recommendations for Preparing the CFS

| Count | No. | Recommendation | Status of recommendation ^a | |
|--|------|--|---|---------|
| | | | Per Treasury and OMB | Per GAO |
| GAO-04-45 (results of the fiscal year 2002 audit) | | | | |
| 1 | 02-4 | As the Department of the Treasury (Treasury) is designing its new financial statement compilation process to begin with the fiscal year 2004 consolidated financial statements of the U.S. government (CFS), the Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of the Office of Management and Budget (OMB), to develop reconciliation procedures that will aid in understanding and controlling the net position balance as well as eliminate the plugs previously associated with compiling the CFS. | <p>To eliminate or explain adjustments to net position, Treasury eliminates, at the consolidated level, intragovernmental activity and balances using formal balanced accounting entries (via Reciprocal Categories) and analyzes transactions that contribute to the unmatched transactions and balances adjustment i.e., the plug. Major contributors to the plug are transactions with the General Fund (within Reciprocal Category 29).</p> <p>A Treasury task group is currently developing the Schedule of General Fund Authority, with the goal to enter audited data for fiscal year 2013 into the Governmentwide Financial Report System (GFRS) and to remove General Fund transactions from the plug. In the interim, Treasury will separately identify certain General Fund transactions by providing agencies with monthly STAR/CARS (Central Accounting Reporting System) data to facilitate reconciliation on a quarterly basis. In addition, Treasury has revised the guidance related to the appropriate use of "Trading Partner 99" (General Fund). This guidance will be issued in fiscal year 2012, to be effective in fiscal year 2013.</p> <p>Also throughout fiscal year 2012, Treasury will continue to identify and resolve, via communications to, and assistance from, agencies, material differences related to fiduciary, employee benefits, buy/sell and transfer activity through the continued efforts of Treasury focus groups to identify and mitigate root causes and implement short- and long-term solutions.</p> | Open. |

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| Count | No. | Recommendation | Status of recommendation ^a | |
|-------|------|---|--|---------|
| | | | Per Treasury and OMB | Per GAO |
| 2 | 02-6 | As OMB continues to make strides to address issues related to intragovernmental transactions, the Director of OMB should direct the Controller of OMB to develop policies and procedures that document how OMB will enforce the business rules provided in OMB Memorandum M-07-03, Business Rules for Intragovernmental Transactions. | Treasury has taken the lead role for resolving intragovernmental disputes and major differences between trading partners. In fiscal year 2011, Treasury published the updated <i>Intragovernmental Business Rules</i> , which include dispute resolution procedures for trading partner agencies to follow. Treasury's dispute resolution process includes a new Intragovernmental Dispute Resolution Request Form to be certified by federal entity chief financial officers (CFO). Treasury as the enforcer of the updated business rules, working with OMB as necessary, will work with agencies, to help ensure the effectiveness of the dispute resolution process during each fiscal year and will document the resolutions. | Closed. |
| 3 | 02-7 | As OMB continues to make strides to address issues related to intragovernmental transactions, the Director of OMB should direct the Controller of OMB to require that significant differences noted between business partners be resolved and the resolution be documented. | See the status for recommendation No. 02-6. | Closed. |

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| Count | No. | Recommendation | Status of recommendation ^a | |
|-------|-------|--|---|---------|
| | | | Per Treasury and OMB | Per GAO |
| 4 | 02-9 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to design procedures that will account for the difference in intragovernmental assets and liabilities throughout the compilation process by means of formal consolidating and elimination accounting entries. | Treasury has designed and implemented formal consolidating and eliminating procedures with regard to intragovernmental assets and liabilities, but some issues remain. During fiscal year 2012, Treasury is revising existing guidance and policies, and developing new guidance and policies as needed, for these remaining issues. Upon implementation of the revised guidance and policies by the agencies, Treasury's consolidation and elimination accounting entries should effectively account for the difference in intragovernmental assets and liabilities. Final resolution is contingent on fully resolving material intragovernmental differences. See the status for recommendation No. 02-4. | Open. |
| 5 | 02-10 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to develop solutions for intragovernmental activity and balance issues relating to federal agencies' accounting, reconciling, and reporting in areas other than those OMB now requires be reconciled, primarily areas relating to appropriations. | See the status for recommendation No. 02-4. | Open. |
| 6 | 02-11 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to reconcile the change in intragovernmental assets and liabilities for the fiscal year, including the amount and nature of all changes in intragovernmental assets or liabilities not attributable to cost and revenue activity recognized during the fiscal year. Examples of these differences would include capitalized purchases, such as inventory or equipment, and deferred revenue. | Treasury's consolidating procedures request information from the agencies related to asset capitalization and agency advances or deferred revenue to assist in ensuring the proper reporting of this activity. During fiscal year 2012, Treasury will finalize guidance related to intragovernmental capitalized purchases to be effective in fiscal year 2013. See the status of recommendation No. 02-4 and No. 02-9. | Open. |

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| Count | No. | Recommendation | Status of recommendation ^a | |
|-------|-------|---|--|---------|
| | | | Per Treasury and OMB | Per GAO |
| 7 | 02-12 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to develop and implement a process that adequately identifies and reports items needed to reconcile net operating cost and unified budget surplus (or deficit). Treasury should report "net unreconciled differences" included in the net operating results line item as a separate reconciling activity in the reconciliation statement. | These unmatched transactions and balances will be reflected only in the Statements of Operations and Changes in Net Position until intragovernmental differences are materially resolved. At that point, unresolved reconciling items, if any, needed to reconcile net operating cost to the unified budget deficit can be separately identified in the reconciliation statements. See the status of recommendation No. 02-13. | Open. |
| 8 | 02-13 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to develop and implement a process that adequately identifies and reports items needed to reconcile net operating cost and unified budget surplus (or deficit). Treasury should develop policies and procedures to ensure completeness of reporting and document how all the applicable components reported in the other consolidated financial statements (and related note disclosures included in the CFS) were properly reflected in the reconciliation statement. | <p>During fiscal year 2012, Treasury is refining its methodology for reconciling operating revenue to budgetary receipts (a component of the unified budget deficit), in collaboration with agencies, and is in the process of readying the methodology for review and comment from all agencies and GAO.</p> <p>In addition, during fiscal year 2012, Treasury will work with OMB to further identify and define all sources of budgetary receipts reported to STAR/CARS. Treasury will take into account GAO review comments, if any, during finalization of the methodology for the CFS and the resolution of unresolved differences.</p> <p>Lastly, a group formed by the Association of Government Accountants (AGA group) is performing an independent review of the compilation of the reconciliation statement and cash statement and will provide short- and long-term solutions for improving the completeness of these statements and consistency with underlying agency financial statement data. Treasury will consider AGA group's recommendations in revising its reconciliation methodology.</p> | Open. |

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| Count | No. | Recommendation | Status of recommendation ^a | |
|-------|-------|---|--|---------|
| | | | Per Treasury and OMB | Per GAO |
| 9 | 02-14 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to develop and implement a process that adequately identifies and reports items needed to reconcile net operating cost and unified budget surplus (or deficit). Treasury should establish reporting materiality thresholds for determining which agency financial statement activities to collect and report at the governmentwide level to assist in ensuring that the reconciliation statement is useful and conveys meaningful information. | During fiscal year 2012, as Treasury works on its reconciliation methodology, it will request more information from agencies related to certain items in the reconciliation statement due to their reporting of certain activity on a net basis instead of on a disaggregated basis. Based on the results of this work, Treasury will determine what additional information is needed from the agencies. Once all disaggregated information is obtained, Treasury can implement its reporting materiality policy to provide more meaningful and useful information in the CFS. See also the status of recommendation No. 02-13. | Open. |
| 10 | 02-15 | If Treasury chooses to continue using information from both federal agencies' financial statements and Treasury's central accounting and reporting system (STAR), Treasury should demonstrate how the amounts from STAR reconcile to federal agencies' financial statements. | Treasury has chosen to use information from STAR/CARS and has identified material areas where STAR/CARS data does not reconcile to federal agencies' financial statements. Treasury will continue to work on its reconciliation methodology during fiscal year 2012 to further resolve these reconciliation issues. In addition, the reconciliation methodology will be revised pending implementation of the AGA group's recommendations. See also the status of recommendation No. 02-13. | Open. |
| 11 | 02-16 | If Treasury chooses to continue using information from both federal agencies' financial statements and from STAR, Treasury should identify and document the cause of any significant differences, if any are noted. | See the status of recommendation No. 02-13. | Open. |

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|-------|-------|---|--|---------|
| | | | Per Treasury and OMB | Per GAO |
| 12 | 02-17 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to develop and implement a process to ensure that the Statement of Changes in Cash Balance from Unified Budget and Other Activities properly reflects the activities reported in federal agencies' audited financial statements. Treasury should document the consistency of the significant line items on this statement to federal agencies' audited financial statements. | Treasury has chosen to use information from STAR/CARS. During fiscal year 2012, Treasury will continue to work on its reconciliation statement methodology which also affects related line items on the cash statement. Once fully developed, the reconciliation methodology will also provide consistency of significant line items on the cash statement to the underlying federal agencies' audited financial statements. In addition, the reconciliation methodology will be revised pending implementation of the AGA group's recommendations. See also the status of recommendation No. 02-13 and No. 02-15. | Open. |
| 13 | 02-20 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to develop and implement a process to ensure that the Statement of Changes in Cash Balance from Unified Budget and Other Activities properly reflects the activities reported in federal agencies' audited financial statements. Treasury should explain and document the differences between the operating revenue amount reported on the Statement of Operations and Changes in Net Position and unified budget receipts reported on the Statement of Changes in Cash Balance from Unified Budget and Other Activities. | Treasury will refine its reconciliation methodology for reconciling budgetary receipts to net operating revenue during fiscal year 2012. Treasury will again work with the agencies that contribute to the largest unreconciled differences to identify the causes of the differences and to resolve them. Treasury will take into account GAO comments, if any, as it finalizes the reconciliation methodology for resolving these differences, as well as consider the AGA group's recommendations related to the compilation of the reconciliation statement and cash statement. | Open. |

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| Count | No. | Recommendation | Status of recommendation ^a | |
|-------|-------|--|---|---------|
| | | | Per Treasury and OMB | Per GAO |
| 14 | 02-22 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to perform an assessment to define the reporting entity, including its specific components, in conformity with the criteria issued by the Federal Accounting Standards Advisory Board (FASAB). Key decisions made in this assessment should be documented, including the reason for including or excluding components and the basis for concluding on any issue. Particular emphasis should be placed on demonstrating that any financial information that should be included but is not included is immaterial. | During fiscal year 2012, Treasury will address some of the issues raised by FASAB's Reporting Entity Task Force and Treasury is supporting and participating in the task force's efforts to help gain clarity and finality on this issue. | Open. |
| 15 | 02-23 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to provide in the financial statements all the financial information relevant to the defined reporting entity, in all material respects. Such information would include, for example, the reporting entity's assets, liabilities, and revenues. | See the status of recommendation No. 02-22. | Open. |
| 16 | 02-24 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to disclose in the financial statements all information that is necessary to inform users adequately about the reporting entity. Such disclosures should clearly describe the reporting entity and explain the reason for excluding any components that are not included in the defined reporting entity. | See the status of recommendation No. 02-22. | Open. |

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| | | | Per Treasury and OMB | Per GAO |
| 17 | 02-35 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to help ensure that federal agencies provide adequate information in their legal representation letters regarding the expected outcomes of the cases. | During fiscal year 2011, with few exceptions, the agencies provided Treasury and OMB adequate information in their legal representation letters regarding the expected outcomes of the cases. Treasury and OMB will work with the few agencies to provide all required information in fiscal year 2012. Treasury has already held a "lessons learned" meeting related to the fiscal year 2011 process and will work during the year with the Department of Justice (Justice), OMB and GAO and the agencies to determine if further changes in policy and/or guidance (e.g., OMB Memorandum 01-02) is needed for all agencies to provide the required information regarding the expected outcomes of legal cases in their legal representations. | Open. |

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| | | | Per Treasury and OMB | Per GAO |
| 18 | 02-37 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to establish written policies and procedures to help ensure that major treaty and other international agreement information is properly identified and reported in the CFS. Specifically, these policies and procedures should require that federal agencies develop a detailed schedule of all major treaties and other international agreements that obligate the U.S. government to provide cash, goods, or services, or that create other financial arrangements that are contingent on the occurrence or nonoccurrence of future events (a starting point for compiling these data could be the State Department's Treaties in Force). | Agencies are currently required to report contingencies in their financial statements and notes pursuant to generally accepted accounting principles (GAAP) guidance. In addition, OMB Circular A-136, specifically references the inclusion of treaties and international agreements within "Commitments and Contingencies." Further, agencies include specific representations with respect to material liabilities or contingencies in their management representations. In addition, the financial statements of most significant entities and many other federal entities received unqualified audit opinions. However, no additional analysis of treaties has been performed to reasonably ensure that all of the federal government's treaties are considered in agency analyses or that agencies are consistently analyzing treaties for recognition or disclosure. Treasury will annually review agency financial statements, audit reports and management representation letters for any references to treaties and international agreements, and if deemed material will disclose in the CFS. | Open. Until a comprehensive analysis of major treaty and other international agreement information has been performed, Treasury and OMB are precluded from determining if additional disclosure is required by GAAP in the CFS, and we are precluded from determining whether the omitted information is material. |
| 19 | 02-38 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to establish written policies and procedures to help ensure that major treaty and other international agreement information is properly identified and reported in the CFS. Specifically, these policies and procedures should require that federal agencies classify all such scheduled major treaties and other international agreements as commitments or contingencies. | See the status of recommendation No. 02-37. | Open. See the status of recommendation No. 02-37. |

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| Count | No. | Recommendation | Status of recommendation ^a | |
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| | | | Per Treasury and OMB | Per GAO |
| 20 | 02-39 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to establish written policies and procedures to help ensure that major treaty and other international agreement information is properly identified and reported in the CFS. Specifically, these policies and procedures should require that federal agencies disclose in the notes to the CFS amounts for major treaties and other international agreements that have a reasonably possible chance of resulting in a loss or claim as a contingency. | See the status of recommendation No. 02-37. | Open. See the status of recommendation No. 02-37. |
| 21 | 02-40 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to establish written policies and procedures to help ensure that major treaty and other international agreement information is properly identified and reported in the CFS. Specifically, these policies and procedures should require that federal agencies disclose in the notes to the CFS amounts for major treaties and other international agreements that are classified as commitments and that may require measurable future financial obligations. | See the status of recommendation No. 02-37. | Open. See the status of recommendation No. 02-37. |
| 22 | 02-41 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to establish written policies and procedures to help ensure that major treaty and other international agreement information is properly identified and reported in the CFS. Specifically, these policies and procedures should require that federal agencies take steps to prevent major treaties and other international agreements that are classified as remote from being recorded or disclosed as probable or reasonably possible in the CFS. | See the status of recommendation No. 02-37. | Open. See the status of recommendation No. 02-37. |

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| | | | Per Treasury and OMB | Per GAO |
| 23 | 02-129 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to ensure that the note disclosure for stewardship responsibilities related to the risk assumed for federal insurance and guarantee programs meets the requirements of Statement of Federal Financial Accounting Standards (SFFAS) No. 5, Accounting for Liabilities of the Federal Government, paragraph 106, which requires that when financial information pursuant to Financial Accounting Standards Board standards on federal insurance and guarantee programs conducted by government corporations is incorporated in general purpose financial reports of a larger federal reporting entity, the entity should report as required supplementary information what amounts and periodic change in those amounts would be reported under the "risk assumed" approach. | This information was requested from federal agencies for disclosure in the fiscal year 2011 CFS. Treasury will work with agencies to improve the consistency of this disclosure in the fiscal year 2012 CFS and will also monitor the work of the FASAB task force that is reviewing the reporting for risk assumed. | Open. Treasury's reporting in this area is not complete. The CFS should include all major federal insurance programs in the risk assumed reporting and analysis. Also, since future events are uncertain, risk assumed information should include indicators of the range of uncertainty around expected estimates, including indicators of the sensitivity of the estimate to changes in major assumptions. |
| GAO-04-866 (results of the fiscal year 2003 audit) | | | | |
| 24 | 03-6 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to develop a process that will allow full reporting of the changes in cash balance of the U.S. government. Specifically, the process should provide for reporting on the change in cash reported on the consolidated balance sheet, which should be linked to cash balances reported in federal agencies' audited financial statements. | Treasury will analyze cash transactions, and work with its Cash Policy area to achieve complete and consistent reporting of cash transactions, to provide full reporting of the changes in the cash balance of the U.S. government. | Open. Treasury has not established and implemented effective processes and procedures for identifying and reporting all items needed to prepare the Statement of Changes in Cash Balance from Unified Budget and Other Activities. |
| 25 | 03-8 | The Director of OMB should direct the Controller of OMB, in coordination with Treasury's Fiscal Assistant Secretary, to work with the Department of Justice (Justice) and certain other executive branch federal agencies to ensure that these federal agencies report or disclose relevant criminal debt information in conformity with generally accepted accounting principles (GAAP) in their financial statements and have such information subjected to audit. | OMB, working with Treasury, Justice, and certain other agencies, will continue working to address this recommendation. | Open. |
| 26 | 03-9 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to include relevant criminal debt information in the CFS or document the specific rationale for excluding such information. | Treasury will disclose criminal debt information in the CFS if material as reflected in the agencies' financial statements. See the status of recommendation No. 03-8. | Open. |

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| | | | Per Treasury and OMB | Per GAO |
| 27 | 03-11 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to modify Treasury's plans for the new closing package to (1) require federal agencies to directly link their audited financial statement notes to the CFS notes and (2) provide the necessary information to demonstrate that all of the five principal consolidated financial statements are consistent with the underlying information in federal agencies' audited financial statements and other financial data. | Treasury's current CFS compilation process provides for direct linkage from the 35 significant federal agencies audited financial statements to most of the CFS principal statements and to the related note disclosures. However, additional work is needed related to the two budgetary principal financial statements. Treasury will take into account GAO comments, if any, as it develops its reconciliation methodology during fiscal year 2012. Treasury will also consider the AGA group's comments and recommendations to improve the compilation of the reconciliation statement and cash statement. See the status of recommendation No. 02-13 and No. 02-15. | Open. Treasury's process for compiling the CFS generally demonstrated that amounts in the Statement of Social Insurance and the Statement of Changes in Social Insurance Amounts were consistent with the underlying federal entities' financial statements and that the Balance Sheet and the Statement of Net Cost were also consistent with the 35 significant federal entities' financial statements prior to eliminating intragovernmental activity and balances. However, Treasury's process did not ensure that the information in the remaining three principal financial statements was fully consistent with the underlying information in the 35 significant federal entities' audited financial statements and other financial data. |
| GAO-05-407 (results of the fiscal year 2004 audit) | | | | |
| 28 | 04-3 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to require that Treasury employees contact and document communications with federal agencies before recording journal vouchers to change agency audited closing package data. | During fiscal year 2012, Treasury will fully implement and enforce its procedures to document communications to the agencies in the supporting documentation for journal vouchers. | Open. |

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| | | | Per Treasury and OMB | Per GAO |
| 29 | 04-6 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to assess the infrastructure associated with the compilation process and modify it as necessary to achieve a sound internal control environment. | During fiscal year 2011, with the assistance of its contractor, Treasury continued to make improvements to its internal control infrastructure. Treasury updated, and will revise and improve, its standard operating procedures (SOP) to document that key controls are in place at all critical areas of the CFS preparation process. Treasury will monitor and assess its efforts to determine its progress in achieving a sound internal control environment. Also, during fiscal year 2011, Treasury restructured the management of the organization responsible for the CFS compilation process to provide additional oversight and accountability over the year-end CFS process. In addition, during fiscal year 2012, Treasury plans to obtain additional personnel, via details from other agencies, with financial reporting expertise, to assist with enhancements and improvements to internal controls. | Open. |
| GAO-06-415 (results of the fiscal year 2005 audit) | | | | |
| 30 | 05-3 | The Director of OMB should direct the Controller of the Office of Federal Financial Management to consider, in order to provide audit assurance over federal agencies' closing packages, not waiving the closing package audit requirements for any verifying agency in future years, such as Tennessee Valley Authority (TVA). | For fiscal year 2011, OMB did not waive the closing package audit requirements for any verifying agency. In addition, over the last 3 fiscal years, TVA progressively moved closer to submitting its closing package by the required financial reporting deadline and is now submitting the closing package timely. | Closed. |
| GAO-07-805 (results of the fiscal year 2006 audit) | | | | |
| 31 | 06-6 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, working in coordination with the Controller of OMB's Office of Federal Financial Management, to establish effective processes and procedures to ensure that appropriate information regarding litigation and claims is included in the governmentwide legal representation letter. | Treasury, in coordination with OMB and Justice, will work during fiscal year 2012 to establish effective processes and procedures to require that appropriate information regarding litigation and claims is included in the governmentwide legal representation letter. | Open. |

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|---|------|---|---|---|
| | | | Per Treasury and OMB | Per GAO |
| 32 | 06-7 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, working in coordination with the Controller of OMB's Office of Federal Financial Management, to develop a process for obtaining sufficient information from federal agencies to enable Treasury and OMB to adequately monitor federal agencies' efforts to reconcile intragovernmental activity and balances with their trading partners. This information should include (1) the nature and a detailed description of the significant differences that exist between trading partners' records of intragovernmental activity and balances, (2) detailed reasons why such differences exist, (3) details of steps taken or being taken to work with federal agencies' trading partners to resolve the differences, and (4) the potential outcome of such steps. | During fiscal year 2012, Treasury will continue its intragovernmental collection, analysis, and reporting process as enhanced in fiscal year 2011, for obtaining sufficient information from federal agencies to enable Treasury and OMB to adequately monitor federal agencies' efforts to reconcile intragovernmental activity and balances with their trading partners. The information obtained includes (1) the nature and a detailed description of the significant differences that exist between trading partners' records of intragovernmental activity and balances, (2) detailed reasons why such differences exist, (3) details of steps taken or being taken to work with federal agencies' trading partners to resolve the differences, (4) the potential outcome of such steps, and (5) additional information related to their intragovernmental differences that would allow Treasury to correct these differences within GFRS. This effort was successful during fiscal year 2011 in reducing the amount, both on a net and absolute value basis, of the total amount of intragovernmental differences. | Open. Treasury furthered its commitment to resolve differences in intragovernmental activity and balances, for example, by expanding focus groups' monitoring and outreach efforts that involved quarterly analysis and ongoing collaboration with entities to resolve intragovernmental differences. However, we found that a significant number of CFOs continue to cite differing accounting methodologies, accounting errors, and timing differences for material differences with their trading partners. Some CFOs indicated that they did not know the reason for the differences. |
| GAO-08-748 (results of the fiscal year 2007 audit) | | | | |
| 33 | 07-1 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to enhance and fully document all practices referred to in the standard operating procedure (SOP) entitled "Preparing the Financial Report of the U.S. Government" to better ensure that practices are proper, complete, and can be consistently applied by staff members. | Treasury will document all of its current practices for preparing the CFS in the SOP. | Open. |

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| | | | Per Treasury and OMB | Per GAO |
| 34 | 07-2 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to enhance Treasury's checklist or design an alternative and use it to adequately and timely document Treasury's assessment of the relevance, usefulness, or materiality of information reported by the federal agencies for use at the governmentwide level. | Treasury addressed many of GAO's concerns related to the checklist during fiscal year 2011, specifically the inclusion of disclosure items related to the principal financial statements and management's discussion and analysis. | Closed. Over the past few years, Treasury has taken several actions to address this recommendation. To provide recommendations that are better aligned with the current status of remaining deficiencies related to this area, we have (1) closed this recommendation based on Treasury's significant progress and (2) included in this report under "Timely Review and Approval of the Financial Reporting Disclosure Checklist" new recommendations for corrective actions for the remaining deficiencies. |
| 35 | 07-5 | The Director of OMB should direct the Controller of OMB's Office of Federal Financial Management, in coordination with Treasury's Fiscal Assistant Secretary, to develop formal processes and procedures for identifying and resolving any material differences in distributed offsetting receipt amounts included in the net outlay calculation of federal agencies' Statement of Budgetary Resources and the amounts included in the computation of the budget deficit in the CFS. | Treasury will work with OMB to perform this analysis and to develop policies and procedures, as part of developing its reconciliation methodology, to resolve these differences. OMB and Treasury, as applicable, will continue their efforts to implement the completed methodology. Treasury will also be working with OMB to further identify and define all sources of distributed offsetting receipts reported to STAR/CARS. | Open. |
| 36 | 07-9 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB's Office of Federal Financial Management, to develop and implement effective processes for monitoring and assessing the effectiveness of internal control over the processes used to prepare the CFS. | Treasury is in the process of reviewing its documentation of internal control procedures, as completed during fiscal year 2011, to determine what internal control design gaps remain and what further controls are needed related to new or revised procedures. See also the status of recommendation No. 04-6. | Open. |

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| | | | Per Treasury and OMB | Per GAO |
| 37 | 07-10 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, working in coordination with the Controller of OMB's Office of Federal Financial Management, to develop and implement alternative solutions to performing almost all of the compilation effort at the end of the year, including obtaining and utilizing interim financial information from federal agencies. | Treasury is leading a subgroup with governmentwide participation on the OMB Circular No. A-136 subcommittee to determine what information can be obtained during the third and fourth quarters of fiscal year 2012 to facilitate the year-end CFS preparation process. Depending on the results of this effort, Treasury will consider what additional requirements related to third quarter information in fiscal year 2013 are needed to facilitate the year-end compilation effort. | Open. |
| GAO-09-387 (results of the fiscal year 2008 audit) | | | | |
| 38 | 08-01 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to design, document, and implement policies and procedures to identify and eliminate intragovernmental payroll tax amounts at the governmentwide level when compiling the CFS. | During fiscal year 2012, Treasury will evaluate the adequacy of the payroll tax amounts reported in the Monthly Treasury Statement by discussing the methodology for preparing this amount with the providing agency. If deemed adequate, policies and procedures will be modified to reflect the results of the analysis and document how this amount is identified and used when compiling the CFS. | Open. |

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|-------|-------|---|---|---|
| | | | Per Treasury and OMB | Per GAO |
| 39 | 08-02 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to develop, document, and implement processes and procedures for preparing and reviewing the Management's Discussion and Analysis (MD&A) and "The Federal Government's Financial Health: A Citizen's Guide to the Financial Report of the United States Government" sections of the <i>Financial Report of the U.S. Government (Financial Report)</i> to help assure that information reported in these sections is complete, accurate, and consistent with related information reported elsewhere in the <i>Financial Report</i> . | The Office of the Fiscal Assistant Secretary (OFAS) first implemented SOPs concerning the preparation of the MD&A and Citizen's Guide for the fiscal year 2009 <i>Financial Report</i> . Since that time, instances of inaccuracies, inconsistency, and incompleteness have been consistently lower than in prior years. OFAS will update its SOPs as needed to reflect new reporting requirements and/or process improvements. | Closed. Over the past few years, Treasury, in coordination with OMB, has taken several actions to address this recommendation. To provide recommendations that are better aligned with the current status of remaining deficiencies related to this area, we have (1) closed this recommendation based on Treasury's and OMB's significant progress, and (2) included in this report under "Review and Approval of the Financial Report" new recommendations for corrective actions for the remaining deficiencies. |
| 40 | 08-03 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to establish and document criteria to be used in identifying federal entities as significant to the CFS for purposes of obtaining assurance over the information being submitted by those entities for the CFS. | During fiscal year 2011, Treasury and OMB established and documented the criteria to identify all federal entities that are significant to the CFS. | Closed. |
| 41 | 08-04 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary, in coordination with the Controller of OMB, to develop and implement policies and procedures for assessing and documenting, on an annual basis, which entities meet the criteria established for identifying federal entities as significant to the CFS. | During fiscal year 2011, Treasury used the significant entity criteria to assess which entities are considered significant to the CFS, and will perform this assessment on an annual basis. | Open. During fiscal year 2011, Treasury did not properly implement its procedures for assessing which entities meet its criteria for identifying federal entities as significant to the CFS. |

GAO-10-757 results of the fiscal year 2009 audit)

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|----|-------|---|---|---------|
| 42 | 09-03 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to enhance the SOP entitled "Analyzing Agency Restatements" to include procedures for analyzing the overall impact of entities' restatements on the CFS and documenting the analysis and related conclusion. | During fiscal year 2011, Treasury complied with its enhanced procedures for analyzing the impact of entities' restatements on the CFS, documenting its analysis and related conclusions, and correctly incorporating the impact of the entities' restatements into the CFS. | Closed. |
|----|-------|---|---|---------|

**Appendix I: Status of Treasury's and OMB's
Progress in Addressing GAO's Prior Year
Recommendations for Preparing the CFS**

| Count | No. | Recommendation | Status of recommendation ^a | |
|-------|-------|---|--|---------|
| | | | Per Treasury and OMB | Per GAO |
| 43 | 09-04 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to develop, implement, and document procedures for identifying, analyzing, compiling, and reporting all significant accounting policies and related party transactions at the governmentwide level. | Treasury will fully implement its procedures for identifying, analyzing, compiling, and reporting all related party transactions at the governmentwide level in fiscal year 2012 by verifying the related party information received in the closing packages to the agencies' underlying audited financial statements, and will document this verification procedure. In addition, Treasury will monitor the work of FASAB's Reporting Entity Task Force as it relates to related party disclosures. | Open. |
| 44 | 09-06 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to enhance the SOP entitled "Statement of Social Insurance, Social Insurance Note, and Required Supplementary Information" to implement and document procedures for assuring the accuracy of staff's work related to preparing the social insurance information for the CFS. | In fiscal year 2012, Treasury will comply with its enhanced Statement of Social Insurance SOP to document that all the social insurance information in the CFS is consistent with the agencies' social insurance information. | Open. |
| 45 | 09-08 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to implement and document procedures for assuring the accuracy of staff's work related to preparing the Schedule of Differences. | In fiscal year 2011, Treasury improved the implementation and documentation of its procedures to help assure completeness and accuracy of documenting the inconsistencies between the amounts provided by the agencies. | Closed. |
| 46 | 09-10 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to implement and document procedures for assuring the accuracy of staff's work related to performing analytical procedures. | During fiscal year 2012 Treasury will improve the implementation and documentation of its procedures to address remaining GAO issues related to assuring the accuracy of staff's work related to performing analytical procedures, specifically strengthening the explanations for all significant variances found during the year-end analyses. | Open. |

**Appendix I: Status of Treasury's and OMB's
Progress in Addressing GAO's Prior Year
Recommendations for Preparing the CFS**

| Count | No. | Recommendation | Status of recommendation ^a | |
|---|-------|--|---|--|
| | | | Per Treasury and OMB | Per GAO |
| GAO-11-525 (results of the fiscal year 2010 audit) | | | | |
| 47 | 10-01 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to enhance the applicable SOPs to include required steps for assuring conformity with SFFAS No. 33 and the consistency of amounts between the Statement of Net Cost and the Federal Employee and Veteran Benefits Payable (FEVBP) note disclosure. | During fiscal year 2011, Treasury enhanced and implemented the applicable SOPs to verify the conformity with SFFAS No. 33 and the consistency of amounts between the Statement of Net Cost and FEVBP note disclosure. | Closed. Treasury has taken several actions to address this recommendation. To provide recommendations that are better aligned with the current status of remaining deficiencies related to this area, we have (1) closed this recommendation based on Treasury's significant progress and (2) included in this report under "Review of Federal Entities' Financial Information for Inclusion in the CFS" a new recommendation for corrective actions for the remaining deficiencies. |
| 48 | 10-02 | The Secretary of the Treasury should direct the Fiscal Assistant Secretary to implement and document procedures for assuring conformity with SFFAS No. 33 and the consistency of amounts between the Statement of Net Cost and the FEVBP note disclosure. | See the status of recommendation No. 10-01. | Closed. See the status of recommendation No. 10-01. |
| 49 | 10-03 | The Director of OMB should direct the Controller of OMB to enhance its procedures for preparing the appendixes to include required steps to assure the accuracy and consistency of the accompanying information presented in the appendixes to the <i>Financial Report</i> related to the federal government's financial management. | During fiscal year 2011, OMB reported this information on the newly released Performance.gov website and no longer included this in the Other Accompanying Information section of the <i>Financial Report</i> . | Closed. |
| 50 | 10-04 | The Director of OMB should direct the Controller of OMB to enhance its procedures for preparing the appendixes to include required steps to maintain documentation supporting the accompanying information presented in the appendixes to the <i>Financial Report</i> related to the federal government's financial management. | See the status of recommendation No. 10-03. | Closed. |

Sources: GAO, Treasury, and OMB.

^aThe status of the recommendations listed in app. I is as of December 12, 2011, the date of our report on the audit of the fiscal year 2011 CFS.

Appendix II: Comments from the Department of the Treasury



ASSISTANT SECRETARY

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

June 7, 2012

Mr. Gary T. Engel
Director, Financial Management and Assurance
Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Engel:

Thank you for the opportunity to comment on the Government Accountability Office's (GAO) draft report on the Fiscal Year (FY) 2011 audit, GAO-12-529, *MANAGEMENT REPORT, improvements Needed in Controls over the Preparation of the U.S. Consolidated Financial Statements*.

The draft Management Report for the FY 2011 audit identifies 10 new recommendations for improving the Consolidated Financial Statements (CFS) preparation process. We concur with GAO's findings and will use them to continue to improve the central accounting and compilation activities associated with the CFS.

We have made significant progress in enhancing our policies and procedures since the issuance of the FY 2011 audit report and expect to implement additional recommendations by the end of FY 2012. We have closed 12 of the 50 recommendations outstanding from the previous CFS audit reports. We also strengthened the internal controls related to the preparation of the CFS. Our efforts included improved CFS disclosures, enhanced internal control processes and procedures, and the development of more detailed corrective actions to address the recommendations.

We have given great management attention and staff resources to resolve material intra-governmental differences along with developing or improving process controls within FMS and the Federal Program Agencies. Our strategy includes the use of multiple focus groups that have identified both short and long term solutions through analysis of material differences and working closely with agencies to identify root causes of differences. We have dedicated full-time resources to review and strengthen policy and guidance for agency reporting of intra-governmental transactions and have worked collaboratively with other agencies and the audit community to issue a comprehensive policy that will help to resolve the material weakness.

**Appendix II: Comments from the Department
of the Treasury**

Along with implementing new policy, we have developed metrics and scorecards that will provide targeted quarterly feedback to agencies on their performance. These metrics and scorecards should produce improved reporting by agencies as we take a proactive approach to enforcing the policy and encouraging agencies to resolve their differences throughout the year. Through the Dispute Resolution Process Treasury has taken a key role in assisting agencies in resolving long standing differences which complements other changes we are implementing. In addition, the team has identified tools and possible system solutions that will aid in compliance with the policy. We have started agency pilot testing of our electronic internet payment platform for intra-governmental buy-sell transactions. We believe that with continued focus and strengthened policy and guidance, differences will be identified and resolved and repeatable processes put in place so that the material weakness can be closed soon.

Finally, we have determined that during the compilation process, transactions with the General Fund are not consolidated or eliminated. As a result, we have developed General Fund accounts that will provide Treasury with the capability to reconcile to agency financial reporting data. Regular postings in the General Fund will begin this fiscal year, and may help in the FY 2012 consolidation. The implementation of the General Fund will move us closer to resolving another material weakness.

In conclusion, we are appreciative of GAO's recommendations. Thank you, again, for the opportunity to review and comment on the final draft. We look forward to working with you and your staff as we fulfill our commitment to improve Federal financial reporting.

Sincerely,



Richard L. Gregg
Fiscal Assistant Secretary

cc: Daniel Werfel, Comptroller, OMB

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