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November 19, 2004

The Honorable Mike DeWine
Chairman
Subcommittee on the District of Columbia
Committee on Appropriations
United States Senate

Subject: *Posthearing Questions: District of Columbia's Structural Imbalance and Management Issues*

Dear Chairman DeWine:

On June 22, 2004, I testified before your subcommittee on the District of Columbia's structural imbalance and management issues.¹ This letter responds to a request from your staff that I provide answers to follow-up questions from the Honorable Richard Durbin, United States Senate. The questions and answers follow.

MANAGEMENT CHALLENGES

Update on Management Challenges and Possible Improvements

- *Can you provide us with any current insights about whether the District has taken steps to address these concerns, and whether those efforts have produced positive results?*
- *What additional improvements would you like to see?*

As I stated in my June 2004 testimony before your subcommittee, the District of Columbia has made progress in improving management and maintaining fiscal discipline. In fact, it appears the District has made some progress since we issued our comprehensive report—*District of Columbia: Structural Imbalance and Management Issues*—in May 2003 (upon which my June 2004 testimony was based).² For example, District officials have taken steps to balance their budgets for fiscal years 2004 and 2005. Also, the District's bond rating has been upgraded by all of the major rating agencies in part due to the region's improving economy and better financial management.

¹ GAO, *District of Columbia: Structural Imbalance and Management Issues*, GAO-04-908T (Washington, D.C.: June 22, 2004).

² GAO, *District of Columbia: Structural Imbalance and Management Issues*, GAO-03-666 (Washington, D.C.: May 22, 2003).

Further, our recent mandated review of the District's performance and accountability plan for fiscal year 2003 found that the District complied with statutory reporting requirements and that the report provided a comprehensive review of the District's performance.³ We also found that the 2003 performance report provided an update on the following performance management programs.

- The District reported on the expansion of performance-based budgeting to 27 additional agencies. All 77 agencies are expected to be utilizing performance-based budgeting by 2006.
- The District also reported plans to expand its recommendations and court orders tracking system to begin tracking the costs of implementing recommendations and court orders. Originally this system was intended to only track the extent to which recommendations and court orders had been implemented throughout the District.
- In addition, the District reported plans to implement an online budgeting and performance program (Argus) to link agency budgeting and performance reporting. The District expected to implement the program in October 2004 in those agencies that are already using or implementing performance-based budgeting. This system will allow for monthly performance reporting and enhance oversight of agencies' data collection efforts. Through this system, agencies will prepare budget requests based on actual program costs. Further, the system will eliminate an agency's ability to modify performance targets or past performance without management approval.

The District's performance goals represent about 90 percent of its total expenditures. While the District has made steady progress in implementing a more results-oriented approach to management and accountability, actions have not been completed on our prior recommendations related to expanding coverage of goals and measures to all activities within the Mayor's authority, as well as the monitoring of court costs.

Despite the progress that has been made, challenges still remain, as evidenced by several studies and investigations that have been released since the issuance of our May 2003 report. For example, the independent auditor of the District's financial statements for fiscal year 2003 again reported District Medicaid provider accounting and financial reporting as a material weakness.⁴ We highlighted Medicaid management as a major challenge in our May 2003 report. According to the independent auditors' report, certain conditions have hindered the ability of the District of Columbia Public Schools (DCPS) and Department of Mental Health to accurately estimate and record amounts owed from the federal government for eligible services in a timely fashion. This means that the District continues to bear more of the burden of its high Medicaid costs with local funds than necessary and does not fully leverage the permanently enhanced federal Medicaid match (70 percent) that Congress gave it in 1997. Addressing these problems in a timely manner

³ GAO, *District of Columbia: FY 2003 Performance Report Shows Continued Improvements*, GAO-04-940R (Washington, D.C.: July 7, 2004).

⁴ Government of the District of Columbia, Office of the Inspector General, *District of Columbia: Independent Auditors' Report on Compliance and on Internal Control Over Financial Reporting* (Washington, D.C.: Feb. 2004).

has taken on greater significance because the District has proposed eliminating its Medicaid reserve fund in fiscal year 2005 (\$55 million in fiscal year 2004). This reserve was intended to serve as a cushion in the District's budget in the event of less-than-expected federal reimbursement, which had been a significant problem in previous years.

In another example, in September 2003 the DC Appleseed Center for Law and Justice⁵ and Piper Rudnick LLP issued a study on special education problems in DCPS, which we also discussed in our May 2003 report.⁶ The District lacks appropriate special education programs and services, which frequently results in DCPS expending resources to subsidize private school placements and related transportation expenses, as well as the costs associated with due process hearings. According to the DC Appleseed Center for Law and Justice report, these problems are exacerbated by DCPS's inadequate dispute resolution process. The report concluded that DCPS's inability to promptly address parental inquiries and concerns about inadequate special education services and facilities results in anger and mistrust on the part of parents. Responding to parental concerns earlier and more effectively could minimize anger and mistrust, thereby reducing lawsuits, due process hearings, and their related legal costs. The report also laid out recommendations for improving DCPS's dispute resolution process.

Moreover, the District Office of the Inspector General reported in September 2003 that DCPS lost the use of approximately \$4.5 million in federal homeland security funds because it was unable to identify a use for and obligate these funds in a timely fashion.⁷ Although DCPS lost out on the use of these funds, it nonetheless has identified a need for security enhancements totaling \$5.7 million.

As agreed with your staff, we did not conduct updated reviews of or new interviews with officials in District agencies in advance of my June 2004 testimony. Nonetheless, several GAO studies completed since the issuance of our report in May 2003 further describe the status of the District's management challenges. Several select examples of other more recent GAO work related to the District follow. In some cases, GAO has also recommended that certain actions be taken to address management challenges.

- **District-wide management and performance.** In our July 2004 review of the District's performance and accountability report for fiscal year 2003 (described above), we identified certain gaps. Specifically, the 2003 performance report did not include 33 activities that represent 10 percent of the District's budget, including public charter schools (the most significant program activity that lacked goals). Previously, we recommended that the District establish goals for the charter schools and report on progress. District

⁵ The DC Appleseed Center for Law and Justice is an organization that brings together volunteer teams of attorneys and other experts to conduct studies of serious local issues, research and analyze them, develop and publish recommendations for systemic reform, and advocate for solutions.

⁶ DC Appleseed Center for Law and Justice and Piper Rudnick LLP, *A Time for Action: The Need to Repair the System for Resolving Special Education Disputes in the District of Columbia* (Washington, D.C.: Sept. 2003).

⁷ Government of the District of Columbia Office of the Inspector General, *Use of Homeland Security Funds at the District of Columbia Public Schools* (Washington, D.C.: Sept. 2003).

officials told us that goals have been established for the charter schools and will appear in the 2004 performance report. According to the report, most of the remaining program activities relate to particular funds (e.g., the disability compensation fund), and measures are not set for such funds.

- **Medicaid—mental health system.** In March 2004 we issued a report on the status of reforms to the District’s mental health system, which is managed by the Department of Mental Health (DMH), including its enrollment and billing system.⁸ DMH has developed and implemented a comprehensive enrollment and billing system designed to coordinate clinical, administrative, and financial processes. Under this system, a core services agency, which is a DMH-certified provider, enrolls eligible consumers in the District mental health system and develops treatment plans, provides and coordinates services, and bills DMH on a fee-for-service (FFS) basis. This system has two key attributes. First, it links payment directly to treatment planning and services provided. Second, it increases access to certain community-based mental health services, with a significant share of the costs reimbursable by federal Medicaid funds for community-based mental health services. For fiscal year 2003, DMH received \$17.5 million in federal Medicaid funds, and DMH expects further growth in Medicaid revenue. In transitioning to FFS, however, providers have faced challenges managing cash flow in a system that no longer guarantees revenue regardless of performance. In addition, because provider contracts were tied to the FFS billing projections, DMH could not pay claims in 2003 for providers that were delivering more services than had been projected until their contracts were changed. As a result, providers did not always receive claims payments on a timely basis in fiscal year 2003. By August 2003, DMH made the necessary contract changes to allow providers to be paid for the remainder of the fiscal year and, according to senior officials, had a plan in process for fiscal year 2004 to prevent this problem from recurring.
- **Medicaid—program and fiscal integrity.** In July 2004, we issued a report on state and federal efforts to prevent and detect improper Medicaid payments to providers.⁹ Fraudulent and abusive billing practices across the 50 states and the District include billing for services, drugs, equipment, or supplies not provided or not needed. States can generate cost savings by applying certain measures to providers determined to be at high risk for inappropriate billing and by generally strengthening their program controls for all providers. We identified a number of program control approaches and surveyed all of the states and the District on the extent to which they have implemented them. These include time-limited enrollment, on-site inspections, and criminal background checks, as well as increased use of information technology and prescription drug controls. According to our inventory, the District had implemented 9 of these 20 cost-saving approaches.

⁸ GAO, *District of Columbia: Status of Reforms to the District’s Mental Health System*, GAO-04-387 (Washington, D.C.: Mar. 31, 2004).

⁹ GAO, *Medicaid Program Integrity: State and Federal Efforts to Prevent and Detect Improper Payments*, GAO-04-707 (July 16, 2004).

- Public safety and justice—jail facilities.** In August 2004 we issued a report that reviewed the status of health and safety conditions at the District of Columbia’s Jail and Correctional Treatment Facility (CTF) along with its management of capital improvement projects at the facility.¹⁰ We reported that District health inspectors consistently identified problems at the facility regarding air quality, vermin infestation, fire safety, and plumbing (among other things). However, we found that District health inspectors did not always document where deficiencies were identified or exact times and dates when they were identified—making it difficult for CTF officials to determine how prevalent health and safety deficiencies were, whether problems were occurring in the same locations, or whether they changed over time. Further, we found that the District lacked written policies and procedures concerning the management of jail-related capital improvement projects. We recommended that District health inspectors improve the specificity of their reports. We also recommended that the District strengthen management of capital improvement projects by establishing specific time frames for completing work and developing and implementing policies and procedures.
- DCPS—special education.** In September 2003, we issued a report on special education disputes and mediation strategies across the states (including the District).¹¹ Officials told us that disagreements usually arose between parents and school districts over fundamental issues of identifying students’ need for special education, developing and implementing their individualized education programs, and determining the appropriate education setting. We found that most due process hearings were concentrated in five states—California, Maryland, New Jersey, New York, and Pennsylvania—and the District of Columbia. We reported that 2,311 special education disputes occurred in these five states and the District in the year 2000—compared to 709 in all other states combined. Also, the District had 336 due process hearing per 10,000 students, compared with 24 per 10,000 in New York. We also found that dispute resolution activity was generally low relative to the number of students with disabilities.

The District has made and is making real and important progress in addressing its long-term and difficult management challenges. However, more work needs to be done. Sustained progress is needed to address the critical financial, program, and performance management challenges that the District faces across various agencies and program areas.

Link between Structural Imbalance and Management Challenges

- While you note that addressing these management issues could help reduce future budget shortfalls, such improvements will not offset the structural imbalance. I assume that conclusion is not in any way intended to signal that ignoring the management problems is acceptable, but can you please comment further on that?*

¹⁰ GAO, *District of Columbia Jail: Management Challenges Exist in Improving Facility Conditions*, GAO-04-742 (Aug. 27, 2004).

¹¹ GAO, *Special Education: Numbers of Formal Disputes Are Generally Low and States Are Using Mediation and Other Strategies to Resolve Conflict*, GAO-03-897 (Washington, D.C.: Sept. 9, 2003).

Ignoring the management challenges that we and others have identified is not acceptable, nor did we mean to imply this in our report or my testimony. District officials agree that management issues need to be addressed. For example, in the District's formal response to our May 2003 report, the District Chief Financial Officer (CFO) concurred that improved program performance would permit the District to enhance the quality of the services it delivers and position the District to obtain a higher level of federal reimbursement than it currently receives. The CFO also acknowledged that significant opportunities for efficiency improvements exist within District programs and noted that the District is taking some corrective actions.

Nonetheless, it is important to consider certain critical points regarding the District's management challenges and their relationship to the fiscal structural imbalance we confirmed in our report. The models we used to estimate the range of the District's fiscal structural imbalance presume that services are provided with average efficiency. To the extent that a jurisdiction does not deliver services with average efficiency, its actual level of services may actually be below average. Due to a combination of its significant management problems and its substantial structural deficit, the District is likely providing a below-average level of services even though its tax burden is among the highest in the nation. Accordingly, the District's management problems waste resources that it cannot afford to lose and draw resources away from providing even an average level of services.

By addressing the management challenges that GAO and others have identified over the years, the District could free up local funds and possibly gain additional federal funds for use in increasing the level of services to its residents and visitors. For example, improving Medicaid management could allow the District to obtain a greater level of federal Medicaid funding and fully leverage its enhanced Medicaid match. However, management improvements will not offset the underlying structural imbalance because it is caused by factors beyond the direct control of District officials. As a consequence, District officials may face more difficult policy choices than most other jurisdictions in addressing a budget gap between spending and revenues based on current policies.

As we stated in our May 2003 report, by virtue of the District being the nation's capital, justification may exist for a greater role by the federal government to help the District address its structural imbalance. However, this strategy is not without its own risks. For example, significant management problems in the District mean that the aid provided, if not used wisely, could result in more wasteful spending or in the District postponing management reforms. Given its management challenges, it is important that the District establish basic management, performance, and accountability standards to ensure the efficient and effective use of any federal resources. Along these lines, it should continue planned management reforms, including the movement to performance-based budgeting. It should also address management problems and implement recommendations for improvements that have been highlighted by GAO and others.

LEGISLATIVE REMEDIES

- *What guidance can GAO offer as Congress evaluates legislative measures to address the District's fiscal structural imbalance challenge?*
- *What should be included in legislative language that would ensure adequate and appropriate transparency and accountability for the use of any federal contributions that may be authorized to address the structural imbalance?*
- *What safeguards would you recommend be considered as essential elements of any funding proposal?*
- *Using H.R. 4269, the District of Columbia Fair Federal Compensation Act of 2004, as a baseline, what additions would improve that approach?*

Due in part to its substantial structural deficit, the District is likely providing a below average level of services even though its tax burden is among the highest in the nation. As a consequence, District officials may face more difficult policy choices than other jurisdictions in addressing a budget gap between spending and revenues based on current policies. For example, given its existing high tax burdens, further raising taxes would likely worsen its competitive advantage in attracting new businesses and residents to the city rather than surrounding jurisdictions. It would also be difficult to cut services further.

If raising taxes or cutting services is to be avoided, an alternative option District officials might exercise would be to continue deferring improvements to its capital infrastructure. However, this strategy also is not viable in the long run, in that deteriorating infrastructure would of necessity lead to further reductions in the levels and types of services provided and ultimately would necessitate either higher taxes or cuts in services.

Federal policymakers are faced with difficult choices regarding what role they should play, if any, in addressing the District's structural imbalance. Federal policymakers could choose not to address the District's structural imbalance and require local officials to deal with the difficult choices it faces to meet its obligations. This approach recognizes that other jurisdictions also face substantial structural deficits, and District officials are in the best position to decide for themselves the most effective means of balancing trade-offs between high tax burdens and reduced levels of public services for local residents and visitors to the nation's capital.

Alternatively, additional federal assistance for the District could compensate for its structural imbalance. However, this assistance might suggest that some other states, also with sizable structural imbalances, would have an equally sound claim on additional federal assistance. Nevertheless, by virtue of the District being the nation's capital, and the restrictions placed upon it, justification may exist for a greater role by the federal government to help the District maintain fiscal balance. As previously noted, this strategy is not without its own risks. For example, management problems that plague the District mean that the aid provided, if not used wisely, could result in the District simply postponing many management reforms necessary to avoid the wasteful expenditure of much needed resources and would assist in closing current budget gaps. Given its management challenges, the District

must achieve basic management performance and accountability standards to ensure an efficient use of any resources.

In the end, it is up to Congress to decide whether or in what form to provide the District with additional federal assistance to compensate for its structural imbalance. As the Mayor of the District of Columbia discussed in his May 2004 report to the Senate Committee on Appropriations, there are various forms that enhanced federal assistance could take. The Mayor outlined three forms: an unrestricted federal payment, assumption of state-like functions by the federal government, and federal funding that would be targeted for specific purposes as laid out in the District of Columbia Fair Federal Compensation Act of 2004.

No matter what form this assistance might take, it is important for Congress to have assurances that the funds would be spent efficiently and effectively and be used for any intended purposes. These safeguards should be written into any legislation. Specifically, District officials should be required to report to Congress on how they plan to spend the federal assistance and regularly report on how it is being spent. For instance, Congress could require District officials to submit a master plan to Congress on how they intend to spend the federal assistance—before any funds are obligated—and update this plan as circumstances or priorities change. Further, any reports and financial statements should be required to undergo periodic review by independent auditors. In addition, Congress may consider further specifying the types of projects for which federal funds could be used. Congress may also consider a matching requirement to ensure that some local funds continue to be used for infrastructure and capital projects.

Finally, as I discussed in my testimony before your subcommittee, it is of critical importance to have an effective and transparent capital decision-making and management system in place for all District agencies. In my response to the third set of questions that follow, I discuss principles and practices that should be followed to ensure efficient and effective capital decision making and management.

PLANNING AND OVERSIGHT

- *What types of preliminary evaluations should be conducted and what management controls should be in place as a prerequisite for addressing the District's infrastructure needs?*
- *In your oral testimony, you referred to an inventory of infrastructure and noted that what GAO was provided as part of its work was an "incomplete" array. Can you elaborate further and describe any impediments GAO encountered in getting complete information?*
- *What do you suggest would help ensure that the District compiles and maintains an accurate and full inventory of its infrastructure needs and estimates, as well as having in place a fully functional system for tracking investments made and projected future costs?*

If the District were to receive additional federal assistance to compensate for its structural imbalance and enhance its ability to fund capital investments—as is proposed in the District of Columbia Fair Federal Compensation Act of 2004 (H.R. 4269)—it is important that the District follow sound practices in order to avoid the costly management inefficiencies it has experienced in the past. Congress needs assurance that any federal assistance to the District would be spent effectively and efficiently. It is critical to have clear, transparent reporting and accountability mechanisms in place to ensure the proper use of federal funds. One option for Congress would be to require the District to develop and submit for review a set of capital planning and management policies and procedures that would be reliably followed by all District agencies.

Regarding my comments about the District's infrastructure inventory, we had some difficulties obtaining complete and timely information on infrastructure projects that were not recommended for financing due to funding constraints. This emphasizes the importance of the District having systems in place to track information related to all infrastructure projects, including proposed projects not approved for funding.

A key way to ensure that federal capital funds are spent effectively and efficiently is to have a clear capital decision-making and management system in place. Along these lines, GAO has developed an executive guide that identifies organizational attributes that are important to the capital decision-making process as a whole, as well as capital decision-making principles and practices used by leading state and local governments and private sector organizations.¹² These principles and practices could be applied to any District agency or the District as a whole. Key elements of this guidance are to closely link any planned capital investments to a government's or organization's strategic goals and objectives, ensure that effective information systems are in place to support sound decision making and management, and ensure that city leaders to clearly communicate their vision and goals to project managers. Specifically, we have identified five basic principles of effective capital decision making and linked certain practices that leading public and private entities use to carry out each principle.

¹² GAO, *Executive Guide: Leading Practices in Capital Decision-making*, GAO/AIMD-99-32 (Washington, D.C.: December 1998).

We did not examine the District's capital planning and management functions in advance of my June 2004 testimony, and District officials may already be following some of these principles and practices in certain program areas. Nevertheless, the District should consider these principles and practices in ensuring the implementation of an effective, transparent, and reliable system for making capital decisions and managing them from start to finish. Our executive guide contains additional detail on each of these practices along with numerous examples from the leading organizations that we studied.

Principle I: Integrate organizational goals into the capital decision-making process.

- **Conduct comprehensive assessments of needs to meet mission and results-oriented goals and objectives.** Conducting a comprehensive needs assessment or analysis of program requirements is an important first step in an organization's capital decision-making process. A comprehensive assessment of capital needs considers an organization's overall mission and identifies the resources needed to fulfill both immediate requirements and anticipated future needs based on the results-oriented goals and objectives that flow from the organization's mission.
- **Identify current capabilities, including the use of an inventory of assets and their conditions, and determine if there is a gap between current and needed capabilities.** Leading organizations gather and track information that helps them identify the gap between what they have and what they need to fulfill their goals and objectives. To help assess current capabilities and establish a baseline, such organizations maintain automated systems that track the use and performance of existing assets and facilities. Current and accurate information is essential. Some functions performed by asset inventory and tracking systems include (1) identifying asset and facility location and status, (2) tracking and reporting asset and facility condition and deferred maintenance needs, and (3) tracking user satisfaction. Routinely assessing the condition of assets and facilities allows managers and other decision makers to evaluate the capabilities of current assets, plan for future asset replacements, and calculate the costs of deferred maintenance.
- **Decide how best to meet the gap by identifying and evaluating alternative approaches (including noncapital approaches).** Leading organizations consider a wide range of alternatives to satisfy their needs, including noncapital alternatives, before choosing to purchase or construct a capital asset or facility. Managers carefully consider options such as contracting out or divesting the activity the asset would support. When they determine that capital is needed, managers also consider repair and renovation of existing assets. When evaluating alternatives, prudent decision makers also consider the various funding options available to them. They weigh the different impacts of debt financing, engaging in

joint-venture projects, or using current-year appropriations. Leading organizations examine their needs and seriously consider whether capital is needed to fulfill their requirements. They look at two primary issues to evaluate options available to them: (1) whether the function is essential to fulfilling the organization's core responsibilities and (2) whether the organization has the specific expertise to perform the function well and cost effectively.

Principle II: Evaluate and select capital assets using an investment approach.

- **Establish a review and approval framework supported by analyses.** We found that establishing a decision-making framework that encourages the appropriate levels of management review and approval, supported by the proper financial, technical, and risk analyses, is a critical factor in making sound capital investment decisions. A well-thought-out review and approval framework can mean capital investment decisions are made more efficiently and supported by better information. Some leading organizations have review processes in place that determine the level of analysis and review that will be conducted based on the size, complexity, and cost of the project. As part of the capital review and approval process, leading organizations develop a decision or investment package to justify capital project requests. Common categories of information in the packages include links to organizational objectives; solutions to organizational needs; project resource estimates and schedules; and project costs, benefits, and risks. These packages provide decision makers with a valuable tool for analysis and planning at the time the project is being considered. Decision packages are supported by a range of materials. Types of materials include detailed economic and financial analyses, such as cost-benefit analyses and analysis of return on investment.
- **Rank and select projects based on established criteria.** Leading organizations have defined processes for ranking and selecting projects. The selection of capital projects is based on preestablished criteria and a relative ranking of investment proposals. Leading organizations determine the right mix of projects by viewing all proposed investments and existing capital assets as a portfolio. Organizations generally find it beneficial to rank projects because the number of requested projects usually exceeds available funding. Sound criteria help link potential investments to program priorities and desired results.
- **Develop a long-term capital plan that defines capital asset decisions.** Once projects are ranked, they should be put into a long-term capital plan. Leading organizations develop long-term capital plans to guide implementation of organizational goals and objectives and help decision makers establish priorities over the long term. While a plan must respond to changing requirements, it is based on the long-range vision for the organization embodied in its overall strategic plan. Therefore, any year-to-year changes to the capital plan should be driven by strategic

decisions. Leading organizations prepare long-term capital plans to document specific planned projects, plan for resource use over the long term, and establish priorities for implementation. These plans usually cover a 5-, 6-, or 10-year period and are updated either annually or biennially. Long-term planning requires that decision makers rank capital needs and promotes making informed choices about managing the organization's resources and debt. Some leading organizations also prepare long-term asset and facility maintenance plans that are incorporated into their long-term capital plans. This helps decision makers determine whether and when to purchase a new capital asset or continue to maintain an existing one.

Principle III: Balance budgetary control and managerial flexibility when funding capital projects.

- **Budget for projects in useful segments.** One strategy that has been proven to be useful to organizations in dealing with problems posed by full funding in a capped environment is to budget for projects in useful segments. This means that when a decision has been made to undertake a specific capital project, funding sufficient to complete a useful segment of the project is provided in advance. The U.S. Office of Management and Budget has defined a useful segment as a component that either (1) provides information that allows the agency to plan the capital project, develop the design, and assess the costs, benefits, and risks before proceeding to full acquisition (or canceling the acquisition) or (2) results in a useful asset for which the benefits exceed the costs even if no further funding is appropriated. For full up-front funding and the funding of useful segments to be effective, organizations must be able to develop good, firm cost estimates of the full cost of either the project or the segments early in the life of the project. To develop these estimates, the organization must have good information and data systems in place. Some organizations fund capital projects in useful or meaningful phases by breaking up their capital planning and budgeting cycles into segments, such as predesign, design, and construction. Funding is provided for one of these segments at a time and generally is not guaranteed from one phase to the next.
- **Consider innovative approaches to full up-front funding.** Alternative strategies used by some leading organizations and federal agencies to accommodate full funding of capital projects in a constrained budget environment include contracting out for capital-intensive services, using an investment component that is similar to a savings account, and developing public/private partnerships. These strategies enhance an organization's flexibility to finance the full costs of projects without compromising management's ability to make decisions based on full costs.

Principle IV: Use project management techniques to optimize project success.

- **Monitor project performance and establish incentives for accountability.** Successful implementation of a capital investment

project is determined primarily by whether the project was completed on schedule, came in within budget, and provided the benefits intended. However, the first step is to provide decision makers with good information about costs, risks, and scope of a planned project *before* committing substantial resources to it. This, in combination with full up-front funding, can help to prevent cost overruns, project cancellations, and projects that fail to meet completion schedules. By monitoring project performance against cost, schedule, and performance goals—as well as establishing incentives to meet those goals—organizations can increase the likelihood that projects will be successfully completed. Typically, a good project plan is used to manage and control project implementation and includes performance measurement baselines for schedule and cost, major milestones, and target dates and risks associated with the project. Regular review of the status of cost, schedule, and performance goals by individuals outside the project team allows for an independent assessment of the project. Leading organizations also establish incentives to encourage teams to meet project goals. Leading organizations generally hold managers accountable for meeting goals. Further, leading organizations use a number of built-in incentives for managers and teams to meet project goals. Among them are reporting project status to individuals or groups in positions of authority outside the project and using the project manager’s overall performance in determining the assignment to future projects.

- **Use cross-functional teams to plan for and manage projects.** Leading organizations use multidisciplinary teams, consisting of individuals from different functional areas led by a project manager, to plan and manage capital projects. Teams typically consist of people from the user community and from the organization’s budget, accounting, engineering, procurement, and other functions. A core project team is established early in the life cycle of a project and additional individuals with particular technical or operational expertise are incorporated during appropriate phases of the project. Moreover, successful teams have spirit, trust, and enthusiasm and a sense of ownership over the project.

Principle V: Evaluate results and incorporate lessons learned into the decision-making process.

- **Evaluate results to determine if organizationwide goals have been met.** One way of determining if a capital investment achieved the benefits that were intended is to evaluate its performance using measures that reflect a variety of outcomes and perspectives. By looking at a mixture of hard and soft measures, for example, financial improvement and customer satisfaction, managers are able to assess performance based on a comprehensive view of the needs and objectives of the organization. To implement this balanced approach to performance measurement, leading organizations developed financial and nonfinancial criteria for success that link to the organization’s overall goals and objectives. Another way to determine if a capital investment is contributing to the success of an

organization's goals and objectives is to conduct an audit after the project is completed. The primary focus is not to evaluate the technical aspects of the project, but rather to evaluate the process and whether the end users are satisfied. The lessons learned from the audit can be incorporated into the design and construction of the next project.

- **Evaluate the decision-making process: reappraise and update to ensure that goals are met.** Although some organizations evaluate their capital decision-making process on an ongoing basis, this is not the norm. Leading organizations seemed generally to revise the processes in response to an internal crisis, such as severe budget constraints, or to a perception of changing needs, a changing environment, or both. In such situations, organizations felt that they had to conduct self-assessments and undergo major changes in their capital decision-making practices in order to continue successful operations.

We are also sending this report to the Honorable Mary Landrieu, Ranking Minority Member of your subcommittee; the Honorable Richard Durbin, United States Senate; the Honorable Eleanor Holmes Norton, House of Representatives; and the Subcommittee on the District of Committee, Committee on Appropriations, House of Representatives. This report is also available to other interested parties at <http://www.gao.gov>.

For additional information on our work on the District of Columbia's fiscal imbalance and management issues, please contact me at (202) 512-6806 or daltonp@gao.gov. Individuals making contributions to this report were Thomas Yatsco, Jeanette Franzel, Norma Samuel, Linda Elmore, Jerry Fastrup, and James Wozny.

Sincerely yours,



Patricia A. Dalton
Director, Strategic Issues

450372