

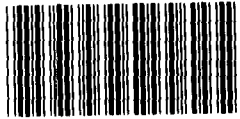
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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

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STATEMENT OF
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ACCOUNTING AND FINANCIAL MANAGEMENT DIVISION
UNITED STATES GENERAL ACCOUNTING OFFICE
BEFORE THE
SUBCOMMITTEE ON INSULAR AFFAIRS
AND THE
SUBCOMMITTEE ON PUBLIC LANDS AND NATURAL PARKS
COMMITTEE ON INTERIOR AND INSULAR AFFAIRS
HOUSE OF REPRESENTATIVES
ON THE
ORGANIZATION AND FUNCTIONS OF THE
U.S. GOVERNMENT COMPTROLLERS

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Mr. Chairman and Subcommittee members, we are here at your request to discuss the results of our ongoing review of the organization and functions of the U.S. Government Comptrollers in American Samoa; Guam (which includes responsibility for the Northern Mariana Islands and the Trust Territory of the Pacific Islands); and the Virgin Islands. With me is Mr. Charles W. Culkin, Jr., Project Manager from our Far East Branch in Honolulu, Hawaii. Our effort is not yet complete and the tentative conclusions and recommendations are still subject to internal review and approval.

My testimony today will summarize the major issues addressed in our draft report entitled "The Audit Function in the Territories Should Be Strengthened," which is currently out with the affected agencies and territorial governments for comment. In summary, our draft discloses that although the audit function presently performed by the Comptrollers should continue, it needs to be strengthened. Transferring the Comptrollers' statutory audit function to Interior's Office of the Inspector General would make the audit function more independent, and also more effective. The audit function could be further strengthened if the preparation of the legislatively mandated "annual report of the fiscal condition of the government" and the audit of that report were made the responsibility of the territorial governments rather than the Comptrollers. Further, more attention could be given Federal grant audits if OMB designated Interior's Inspector General as the cognizant Federal audit agency under the single audit concept.

However, a strengthened Federal audit presence alone is not enough to improve the economy and efficiency of the territorial governments. We believe, they need to assume greater responsibility for establishing and maintaining strong financial management systems, establishing audit followup systems, and strengthening their own internal audit capabilities.

DUTIES AND RESPONSIBILITIES
OF THE COMPTROLLERS

The organic act for Guam and that for the Virgin Islands establishes the position of a Government Comptroller. A Secretarial Order issued by the Secretary of the Interior establishes the position of Government Comptroller for American Samoa. All the Comptrollers are appointed by the Secretary of the Interior.

The Comptrollers are responsible for auditing all significant aspects of governmental operations and Federal programs in the territories. The basic objective of the Comptrollers' audit activities is to (1) improve the efficiency, economy, and effectiveness of territorial programs and (2) ensure that the substantial Federal funds covered into territorial treasuries are properly accounted for and audited. Until recently, the Comptrollers have also provided technical assistance to improve territorial financial management systems.

In approving the legislation that created the position of Government Comptroller for Guam, the House Committee on Interior and Insular Affairs noted the continuing interest of the Federal Government in the operation of the territorial government,

including direct and indirect Federal financial assistance, and the fact that the elected Governor would function without any direct supervision from the executive branch of the Federal Government (H. Rept. 90-1521, June 5, 1968, on H.R. 7329). A similar justification supported the establishment of the position of Government Comptroller for the Virgin Islands. In addition, the committee took the position that the function of the Comptroller is only that of an auditor, and not a policymaker, by specifically stating that the Comptroller is not to interfere with the administration of the executive branch of the territorial government.

ACTION NEEDED TO ENSURE THAT A FEDERAL
AUDIT PRESENCE CONTINUES IN THE TERRITORIES

Although the territories have made substantial progress toward self-government in recent years, a Federal audit presence is still needed to ensure that the substantial Federal financial assistance provided to the territories to operate their governments, finance their capital improvements, and develop their economies is accounted for and audited. In fiscal 1981, Federal assistance totaled about \$615 million, or 81 percent of the total territorial budget.

The need for Federal audit is further evidenced by the fact that major deficiencies still exist in territorial financial management systems. For example, the territorial governments are experiencing problems in eliminating delays in processing financial documents, developing accounting and physical controls over fixed assets, and providing separate accountability for

various funds. Also, they are not performing periodic general ledger account reconciliations to ensure that account balances are correct and/or agree with subsidiary ledgers.

In addition, unless some action is taken before the impending termination of the U.S. administration of the Trust Territory of the Pacific Islands, there will no longer be a Federal audit presence in the Northern Mariana Islands, and a diminished Federal audit presence in the new governments of the Marshall Islands, the Federated States of Micronesia, and Palau. In view of the substantial Federal assistance these governments will receive in future years and the serious financial management problems they are currently experiencing, we believe that a continuous Federal audit presence is needed.

TRANSFER OF FEDERAL AUDIT FUNCTION
TO INTERIOR'S INSPECTOR GENERAL
WOULD ENHANCE INDEPENDENCE

Our review showed that the independence of the Comptrollers' audit function has been impaired because they do not report to a high enough level in the Department of the Interior and because they are located in a line organization which has management responsibility for the activities being audited. This could easily be addressed by transferring the audit function to the Inspector General who reports to the Secretary.

In addition to organizational impairments to independence, we found that the establishment of close relationships between auditors and territorial officials and the auditing of programs by the same individuals who also provided technical assistance

on the programs, may have affected the Comptrollers' ability to do work and report findings in an impartial manner. Also, the Comptrollers' independence has been impaired by external factors, including restricted access to records and information, limited staff resources, and delayed territorial government responses to audit reports.

We believe, however, that most of these personal and external impairments to independence would be eliminated and others could be substantially reduced, if the Comptrollers' audit function was transferred to the Inspector General. Most importantly, auditors would no longer have to audit territorial programs and operations on which they provided technical assistance, because program operating responsibilities are prohibited under the Inspector General Act. In addition, close relationships with territorial officials could be substantially reduced by having the Inspector General institute a program of rotating auditors periodically. Such a program would enable the audit staff to broaden their professional auditing experience and training. Access to records and information would be improved because the Inspector General must report to the Congress semiannually on his audit findings and recommendations.

In addition, we believe the audit function would be more effective under the Inspector General. As part of a professional audit organization, the audit function would receive the professional level of technical guidance and direction required to effectively carry out an audit operation. The Inspector General

would be able to provide the necessary oversight, review, and assistance in developing comprehensive audit plans; following up on audit findings and recommendations; ensuring compliance with audit standards; determining audit staff resources; providing audit staff training programs; developing audit staff rotation programs; and recruiting audit staff.

EFFECTIVENESS OF AUDIT FUNCTION
NEEDS TO BE IMPROVED

In addition to the problems previously discussed regarding the need to (1) ensure a continuing Federal audit presence and (2) transfer the audit function to Interior's Inspector General, we also found that the adequacy of the audit coverage was weak and needed improvement. The lack of effectiveness stems from the following three problems.

--A large portion of the limited resources available are devoted to preparing a legislatively mandated "annual report of the fiscal condition of the government." We found that the nature and purpose for the report is ill defined and, since it is not developed in a timely manner, it is of little value to the users.

--Very few Federal grant programs in the territories are audited.

--The lack of a formalized audit followup system has resulted in infrequent followup on audit recommendations.

We believe the audit function in the territories would be further strengthened if the preparation of the legislatively required annual report and the annual audit of that report were

made the responsibility of the territorial governments. Relieving the Federal auditors of the annual report requirement would enable them to increase their audit coverage of territorial programs and operations. In particular, more attention could be given to Federal grant audits. Also, if OMB designated the Inspector General as the cognizant Federal audit agency under the single audit concept, there would be organizationwide audit coverage of Federal grant programs.

Furthermore, there is a need to establish formalized report followup systems to monitor corrective actions taken by the territorial governments on the Federal auditors' findings and recommendations. Requiring the territorial Governors to submit a written statement of actions taken on Federal audit recommendations would help the Federal auditors and the territorial governments improve the economy and efficiency of territorial operations and ensure better accountability over Federal and local funds.

MORE FEDERAL TECHNICAL ASSISTANCE AND
ASSUMPTION OF GREATER RESPONSIBILITY BY THE
TERRITORIES WOULD ENHANCE AUDIT EFFECTIVENESS

Although the focus of our review was on the Federal audit function in the territories, it is clear that a strengthened Federal audit presence alone is not enough to improve the economy and efficiency of the territorial governments. They need to assume a greater responsibility for establishing and maintaining strong financial management systems to ensure proper control and accountability over Federal and local funds. Although

this is primarily the territorial governments' responsibility, they cannot do the job alone; they need Federal technical assistance.

The Interior's Office of Territorial and International Affairs technical assistance branches represent a permanent local technical assistance capability in the territories. However, as of May 15, 1981, these offices only had 11 staff members working with the territorial governments in correcting their financial management problems. While we did not specifically review the Office of Territorial and International Affairs technical assistance activities, the extent of territorial financial management problems described earlier in my testimony is such that we question the sufficiency and effectiveness of the Office of Territorial and International Affairs current and past technical assistance.

Some territorial leaders and financial management officials told us they hoped the Office of Territorial and International Affairs would develop a comprehensive technical assistance action plan and provide all the necessary resources--staff and/or funds--so that their territorial governments could establish and maintain effective financial management systems. In addition, we believe such assistance should also be provided to the new governments of the Marshall Islands, the Federated States of Micronesia, and Palau. These governments, who have experienced difficulties under the Trust Territory of the Pacific Islands financial management system are considering establishing their own financial management systems.

In addition, we believe territorial audit followup systems are needed to assure that all Federal and independent audit report recommendations are identified and corrective actions are implemented and followed through to completion. Furthermore, increasing the size of internal audit staffs, improving staff capabilities, expanding the scope of audit coverage, and ensuring audit independence would clearly assist the territorial and Federal Governments in improving the economy and efficiency of territorial operations and ensuring accountability over Federal and local funds.

Our draft report suggests a number of actions by the Congress for legislative changes as well as administrative actions to be taken by the executive agencies and territorial governments.

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Mr. Chairman, this concludes my statement. We will be pleased to answer any questions you or other members of the Subcommittee may have.

**ANTICIPATED FEDERAL ASSISTANCE
AND TERRITORIAL REVENUES
FISCAL 1980-1982
(dollars in millions)**

	<u>American Samoa</u>			<u>Guam</u>			<u>Northern Mariana Islands</u>			<u>Trust Territory of the Pacific Islands</u>			<u>Virgin Islands</u>			<u>Total</u>		
	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>
FEDERAL ASSISTANCE																		
Direct Interior appropriations	\$17.3	\$25.8	\$23.7	\$ 10.2	\$ 12.0	\$ 10.0	\$27.1	\$24.4	\$23.6	\$120.0	\$ 94.4	\$ 72.5	\$ 21.0	\$ 9.8	\$ 18.2	\$195.6	\$166.4	\$148.0
Federal grants	16.9	14.5	15.2	57.3	65.0	55.0	12.7	17.9	18.0	37.8	35.0	30.0	80.0	88.6	60.6	1/204.7	221.0	178.8
Taxes "covered over" by Treasury Department	-	-	-	17.7	18.5	19.5	-	-	-	-	-	-	29.0	36.0	36.0	46.7	54.5	55.5
Income taxes in lieu of Federal taxes	15.5	15.3	15.0	62.9	68.0	70.0	-	-	-	-	-	-	86.2	90.0	93.6	164.6	173.3	178.6
	\$49.7	\$55.6	\$53.9	\$148.1	\$163.5	\$154.5	\$39.8	\$42.3	\$41.6	\$157.8	\$129.4	\$102.5	\$216.2	\$224.4	\$208.4	\$611.6	\$615.2	\$560.9
TERRITORIAL REVENUES																		
Other local taxes and nontax revenues	4.5	4.7	5.0	36.8	45.4	45.8	9.2	10.6	10.9	13.9	14.6	15.6	63.9	65.6	67.3	128.3	140.9	144.6
Total revenues	\$54.2	\$60.3	\$58.9	\$184.9	\$208.9	\$200.3	\$49.0	\$52.9	\$52.5	\$171.7	\$144.0	\$118.1	\$280.1	\$290.0	\$275.7	\$739.9	\$756.1	\$705.5
PERCENTAGE FEDERAL ASSISTANCE TO TOTAL REVENUES																		
	92	92	92	80	78	77	81	80	79	92	90	87	77	77	76	83	81	80

SOURCE: U.S. Department of Interior, Office of Territorial and International Affairs