

GAO

Testimony

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Financial Management, Committee on Government  
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INSPECTORS GENERAL

Enhancing Federal  
Accountability

Statement of David M. Walker  
Comptroller General of the United States





Highlights of [GAO-04-117T](#), a testimony before the Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform, House of Representatives

## Why GAO Did This Study

On the 25th anniversary of passage of the Inspector General (IG) Act, the Subcommittee sought GAO's views on the role of the IGs in providing independent oversight within federal agencies and to discuss the new and continuing challenges faced by government performance and accountability professionals.

## What GAO Recommends

In order to enhance the effectiveness of federal accountability professionals, Congress may wish to consider establishing, through statute, a small group of designated federal accountability officials, such as representatives from GAO and IG councils, to develop and implement a periodic strategic planning and ongoing coordination process for the manner in which GAO and IG work will be focused to provide oversight to high-risk areas and significant management challenges across government, while leveraging each other's work and minimizing duplication.

Congress may also want to consider enacting legislation making agencies responsible for paying the cost of their financial statement audits.

Congress may also wish to consider restructuring the IGs, which would include elevating certain IGs to presidential appointment and consolidating specific IG offices where benefits can be shown.

[www.gao.gov/cgi-bin/getrpt?GAO-04-117T](http://www.gao.gov/cgi-bin/getrpt?GAO-04-117T). To view the full product, click on the link above. For more information, contact Jeanette Franzel at (202) 512-9406 or [franzelj@gao.gov](mailto:franzelj@gao.gov).

# INSPECTORS GENERAL

## Enhancing Federal Accountability

### What GAO Found

The IGs have made a significant difference in federal performance and accountability during the past 25 years as indicated by their reports of billions of dollars in savings to the public and numerous civil and criminal referrals. They have earned a solid reputation for preventing and detecting fraud and abuse; promoting improvements in government operations; and providing helpful analyses on a host of governmentwide initiatives.

Notwithstanding the accomplishments of the past, our nation now faces new challenges that demand even more from government performance and accountability professionals. For example, we are fighting international terrorism while facing a large and growing structural deficit. In addition, recent corporate failures have shaken public confidence in financial reporting and accountability in the private sector. Federal auditors can learn important lessons from the accountability breakdowns in the private sector and the resulting legislation passed by Congress.

Closer strategic planning and ongoing coordination of audit efforts between GAO and the IGs would help to enhance the effectiveness and impact of work performed by federal auditors. Working together and in our respective areas of expertise in long-term challenges and agency-specific issues, GAO and the IGs can provide useful insights and constructive recommendations on a broad range of high-risk programs and significant management challenges across government.

A practical issue that has arisen is who pays the cost of agency financial statement audits. Many IGs have told us that the cost of agency financial audits has taken resources away from their traditional work. In the private sector, the cost of financial audits is a routine business expense borne by the entity being audited and represents a small percentage of total expenditures for the audited entity.

In a prior study, we considered the benefits of consolidating the smallest IG offices with those of presidentially appointed IGs and converting agency-appointed IGs to presidential appointment where their budgets were comparable. We believe that, if properly implemented, conversion or consolidation of IG offices could increase the overall independence, economy, efficiency, and effectiveness of IGs.

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Mr. Chairman and Members of the Committee:

I appreciate the opportunity to share my thoughts with you on the important role of the Inspectors General (IG), established in statute 25 years ago this month to provide independent oversight within federal agencies. More significant for this discussion than the anniversary of landmark legislation, however, are the new and continuing challenges we face in assuring open, honest, effective, and accountable government and the critical role of the IGs, in partnership with GAO and other performance and accountability organizations, in addressing these challenges.

A quarter of a century ago, Congress established statutory IGs in response to serious and widespread internal control breakdowns in major government departments and agencies, questions about integrity and accountability in government as a whole, and failures of oversight in the federal government. The IGs established by the Inspector General Act of 1978 (IG Act) were charged with preventing and detecting fraud and abuse in their agencies' programs and operations; conducting audits and investigations; and recommending policies to promote economy, efficiency, and effectiveness. The IG Act fortified the position of IG with provisions protecting independence, provided powers of investigation, and mandated reporting not just to the agency head but to Congress as well. (See app. I for a more detailed history of the IG Act.)

In the years since passage of the IG Act, Congress has also enacted a series of laws to establish a foundation for efficient, effective, and accountable government. This body of legislation has given IGs new responsibilities and greater opportunities to play an increasing role in government oversight. Clearly, the IGs have made a significant difference in federal performance and accountability during the past 25 years as indicated by their reports of billions of dollars in savings to the public and thousands of recommendations and civil and criminal referrals. They have earned a solid reputation for preventing and detecting fraud, waste, and abuse; promoting improvements in government operations; and providing helpful analyses on a host of governmentwide initiatives. It is safe to say that the federal government is a lot better off today because of the IGs' efforts.

Notwithstanding the accomplishments of the past, we now face continuing challenges that demand even more from government performance and accountability professionals. For example, our nation is fighting international terrorism while much of the critical government infrastructure that we are trying to protect dates back to the 1950s. At the

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same time, this nation is facing a large and growing structural deficit due primarily to known demographic trends and rising health care costs. Recent corporate failures have shaken public confidence in financial reporting and accountability in the private sector. In response, Congress passed the Sarbanes-Oxley Act of 2002, which has significant new requirements for publicly traded companies and their auditors. Federal auditors can learn important lessons from the accountability breakdowns in the private sector and the resulting legislation passed by Congress.

We have achieved many important successes in working across organizational lines with the IGs and state and local government auditors. An important recent effort in building closer ties in the government accountability community has been the domestic working group, which I established in 2001 to bring together key staff from GAO, the IGs, and state and local audit organizations to explore issues of mutual interest and concern. The annual roundtable discussions and interim activities of the domestic working group help to focus attention on key issues and shared challenges facing the government audit community and allow participants to compare notes on methods, tools, benchmarking results, and best practices. In the early 1970s, GAO organized the intergovernmental audit forums in cooperation with federal, state, and local audit organizations. These forums provided the means through which new intergovernmental audit relationships were developed and improved the usefulness of auditing at each level of government. Some IGs have become active participants with GAO at the forums to provide a means for exchanging views, solving common problems, and promoting the acceptance and implementation of government auditing standards. Other IGs, however, have not been very involved in these forums and, in my view, this needs to change.

In addition, we have had the active participation of many IGs and state and local government auditors on the Comptroller General's Advisory Council on Government Auditing Standards. The Council provides advice and guidance on revisions to the Comptroller General's *Government Auditing Standards*, commonly known as the "Yellow Book," which is used by government auditors at the federal, state, and local levels, as well as contracted independent public accountants (IPA), in the audits of government programs and activities. It is time, however, for IGs and other members of the federal accountability community to build on past successes by putting additional focus and efforts on reaching across institutional lines and forming new alliances to address the complex challenges facing our government and our nation.

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My statement today will focus on five main points:

- opportunities for increasing the effectiveness of the federal performance and accountability community through an enhanced strategic partnership between the IGs and GAO,
- coordination of the IG and GAO roles in agency financial statement audits and the audit of the U.S. government's consolidated financial statements,
- the IG role in federal financial management advisory committees,
- structural streamlining within the IG community to increase resource efficiencies, and
- matters for congressional consideration to enhance federal performance and accountability.

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## The Need for an Enhanced Strategic Partnership between the IGs and GAO

One of the challenges facing the federal performance and accountability community today is the need to meet increasing demands and challenges with our current resources. Key to this challenge is determining how GAO and the IGs can best complement each other and coordinate their efforts. The IG Act requires that the IGs coordinate with GAO to avoid duplicating efforts. In practice, GAO has largely devoted its efforts to program evaluations and policy analyses that look at programs and functions across government, and with a longer-term perspective; at the same time, the IGs have been on the front line of combating fraud, waste, and abuse within each agency, and their work has generally concentrated on issues of immediate concern with more of their resources going into uncovering inappropriate activities and expenditures through an emphasis on investigations. GAO and the IGs are, in many respects, natural partners. We both report our findings, conclusions, and recommendations to Congress. As I mentioned earlier, we share common professional audit standards through the Yellow Book, and I am proud to say that several current IGs and many of their staff are GAO alumni, including the Honorable Gaston Gianni, the IG of the Federal Deposit Insurance Corporation and Vice-Chair of the President's Council on Integrity and Efficiency, and Barry Snyder, the IG of the Federal Reserve Board and Vice-Chair of the Executive Council on Integrity and Efficiency, who are on the panel following me today.

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While GAO and the IGs make up the federal performance and accountability community, the division of responsibilities between them has not generally included, nor does the IG Act include, strategic planning and allocation of work across government programs based on risk and the relative competitive advantages of each organization. Traditionally, GAO and IG coordination has been applied on an ad-hoc, job-by-job or issue-by-issue basis. We now have both the need and the opportunity to enhance the effectiveness of federal oversight through more strategic and ongoing coordination of efforts between GAO and the IGs in the following areas:

- addressing major management challenges and program risks,
- monitoring the top challenges the government faces, such as implementation of the President's Management Agenda, and
- conducting the audit of the government's consolidated financial statements.

Later in this testimony, I am suggesting that Congress consider establishing, through statute, assignment of responsibility to a select group of designated federal accountability and performance professionals to engage in a formal, periodic strategic planning and ongoing engagement coordination process to focus federal audit efforts across the federal government. This process would be in addition to, and would not replace, the current coordination of information sharing and technical cooperation being implemented by the domestic working group, the audit forums, and the President's Council on Integrity and Efficiency (PCIE) and the Executive Council on Integrity and Efficiency (ECIE).<sup>1</sup>

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## Major Management Challenges and Program Risks

GAO's latest high-risk report,<sup>2</sup> released in January 2003, highlights areas across government that are at risk either due to their high vulnerability to waste, fraud, abuse, and mismanagement, or as major challenges associated with the economy, efficiency, and effectiveness of federal programs, policies, processes, functions, or activities. Many of the high-risk

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<sup>1</sup>These councils were established by Executive Order and are described later in this testimony.

<sup>2</sup>U.S. General Accounting Office, *High Risk Series: An Update*, [GAO-03-119](#) (Washington, D.C.: January 2003).

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areas we identified involve essential government services, such as Medicare and mail delivery, that directly affect the well-being of the American people. Although some agencies have made strong efforts to address the deficiencies cited in the high-risk reports—and some of the programs included on GAO’s initial high-risk list in 1990 have improved enough to warrant removal—we continue to identify many other areas of high risk. Greater strategic coordination between GAO and the IGs on a plan for monitoring and evaluating high-risk issues and keeping the pressure high to reduce the risk of these programs is not only desirable, it is essential if we are to reduce the risk of key government programs.

At the request of Congress, the IGs annually report issues similar to those in GAO’s high-risk report identifying the “Top Management Challenges” facing their agencies. In fiscal year 2002, the IGs ranked information technology, financial management, and human capital management among the most important challenges confronting their agencies governmentwide; other priorities included performance management, public health and safety, and grants management. Each of these areas closely corresponds to an area on GAO’s high-risk list.

Although both GAO and the IGs have efforts in place to identify major risks and challenges within government, there is no mechanism in place to carry out an integrated, strategic planning process as a means through which these issues will be monitored and evaluated in the future through combined and coordinated GAO and IG oversight.

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## President’s Management Agenda

The administration has signaled its commitment to government transformation with the President’s Management Agenda (PMA), which targets 14 of the most glaring problem areas in government for immediate action. Five areas—strategic human capital, budget and performance integration, improved financial performance, expanded electronic government, and competitive sourcing—are governmentwide in scope, while 9 are agency specific. Each area has the potential for dramatic improvement and concrete results. The areas also reflect many of the concerns raised by both GAO’s high-risk report and the IGs’ top management challenge lists. So far, however, progress on PMA has been uneven. To achieve consistent progress, sustained attention from Congress, the administration, and the agencies is needed. I believe that GAO and the IGs can make important contributions, using our combined experience, to help monitor the implementation of this important initiative.

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Key policymakers increasingly need to think beyond quick fixes and carefully consider what the proper role of the federal government should be in the 21st century. Members of Congress and agency heads can start by undertaking a top-to-bottom review of federal programs and policies to determine which should remain priorities, which should be overhauled, and which have outlived their usefulness or are just no longer affordable given more pressing demands. Everything that forms the government's base must be on the table, including tax, spending, and regulatory policies. Policymakers will need to distinguish "wants," which are optional, from "needs," which can be urgent. They need to make hard choices that take into account what the American people will support and what the federal government can afford and sustain over time. To make informed decisions, Congress and agency heads will require hard facts and professional analyses that are objective, fact based, timely, accurate, nonpartisan, fair, and balanced. GAO and the IGs are important sources of such objective information and analyses.

With our respective areas of expertise in long-term challenges and agency-specific issues, GAO and the IGs can provide useful insights and constructive recommendations on programs that may warrant additional resources, consolidation, revision, or even elimination. Closer periodic strategic planning and ongoing engagement coordination between GAO and the IGs would help to ensure continued effective oversight of these key issues facing government.

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## Audit of the U.S. Government's Consolidated Financial Statements

GAO and the IGs are already partners in one of the most far-reaching financial management initiatives in government—the yearly audits of the federal government's consolidated financial statements. Under the Chief Financial Officers (CFO) Act of 1990 as expanded by the Government Management Reform Act of 1994, the IGs at the 24 agencies<sup>3</sup> named in the CFO Act are responsible for the audits of their agencies' financial statements. In meeting these responsibilities, most IGs have contracted with IPAs to conduct the audits either entirely or in part. GAO is responsible for the U.S. government's consolidated financial statements

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<sup>3</sup>The Federal Emergency Management Agency (FEMA), one of 24 agencies named in the CFO Act, was transferred to the new Department of Homeland Security (DHS), effective March 1, 2003. With the transfer, FEMA will no longer be required to prepare audited stand-alone financial statements under the CFO Act. Consideration is now being given to making DHS a CFO Act agency, which would bring the number of CFO Act agencies back up to 24.



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audit, which by necessity is based largely on the results of the IGs' agency-level audits.

Since 1997, GAO has been unable to give an opinion on the consolidated financial statements, in large part because of continuing financial management problems at several agencies that also have resulted in disclaimers of opinion by some IGs on their agency financial statements—most notably the Department of Defense (DOD). In recent years, we have seen progress in the results of the audits of the CFO Act agency financial statements with more and more IGs and their contracted IPAs moving from issuing a disclaimer of opinion to issuing an unqualified (“clean”) opinion on their respective agency financial statements. In fact, 21 of the 24 CFO Act agencies received an unqualified opinion on their fiscal year 2002 financial statements, up from only 6 agencies for fiscal year 1996. We anticipate that if sufficient progress continues to be made, there is a chance that we may be able to render a qualified opinion on the consolidated balance sheet in a few years as a first step toward rendering an opinion on the full set of financial statements.

Our reviews of the work done by other IGs and IPAs on agency-level financial statement audits during the last 2 years identified opportunities for improvement in sampling, audit documentation, audit testing, analytical procedures, and auditing liabilities. The varying quality of the audit work has been of concern to us because of our need to use the work of the agency auditors to support expressing an opinion on the U.S. government's consolidated financial statements—an opinion for which, in the final analysis, GAO is solely responsible and accountable.

Earlier involvement and access by GAO in the agency-level financial statement audits would help to strengthen the IG and IPA audit process and bolster our ability to use their work in rendering an opinion. At a minimum, GAO needs to (1) be involved up front in the planning phase of each agency-level audit, (2) have unrestricted access to IG and IPA audit documentation and personnel throughout the performance of the audit, (3) receive assurances that each agency-level audit is planned, performed, and reported in conformity with the Financial Audit Manual (FAM) developed jointly and adopted by GAO and the PCIE, and (4) be notified in advance of any planned deviation from the FAM's requirements that could affect GAO's ability to use the agency auditors' work.

At one agency (Department of Energy), for the selected areas we reviewed, we found that the audit work was performed in conformity with the FAM

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and that we would have been able to use the work without having to perform additional audit procedures. The IG has an oversight team composed of senior-level staff who perform moderate-level quality control reviews of the contracted IPA's work throughout the audit process. The oversight team evaluates its IPA in areas such as audit planning and execution, audit documentation, and staff qualifications. These types of practices could be shared and expanded upon across the IG community. As an initial step to make the IG and IPA audit process stronger and enhance GAO's ability to use their work in rendering an opinion, we are considering holding a forum with the IGs and the IPAs to share information—based on GAO's review of the IG and IPA work—regarding best practices and areas to focus on that need additional audit work, and to establish a framework for enhanced coordination of the financial statement audit work.

Changes to enhance the agency financial statement audit process are especially important given the planned acceleration of reporting deadlines for agency audits. Although some agencies accelerated their reports for fiscal year 2002, starting with fiscal year 2004, the Office of Management and Budget (OMB) has required that agencies issue their audited financial statements no later than 45 days after the end of the fiscal year, with the consolidated financial statements to be issued 30 days later. In past years, when the reporting deadlines were 4 and 5 months after the end of the fiscal year, agencies made extraordinary efforts in which they spent considerable resources on extensive ad hoc procedures and made adjustments of billions of dollars to produce financial statements months after the fiscal year had ended. Given the accelerated reporting dates, such extraordinary approaches will no longer be an option. Over the next few years, as the government addresses the impediments to receiving an opinion on its consolidated financial statements, and we move closer to being able to render an opinion on the consolidated financial statements, GAO will need to invest more resources in assuring that the work of the IGs and IPAs on the agency-level financial statement audits can be used by GAO to support the audit of the consolidated financial statements. This resource investment is necessary if GAO is to be able to render an opinion on the consolidated financial statements.

Another matter of concern regarding the audit of the U.S. government's consolidated financial statements involves the approaches used by the IGs and IPAs for reporting on internal control at the agency level. Our position is that an opinion on internal control is important in the government environment and that the public should be able to expect audit assurance on the adequacy of internal control over financial reporting. We believe that

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auditor opinions on internal control are a critical component of monitoring the effectiveness of an entity's risk management and accountability systems. We also believe that auditor opinions on internal control are appropriate and necessary for major public entities such as the CFO Act agencies currently included in the U.S. government's consolidated financial statements.

As does GAO in connection with our own audits, several agency auditors are voluntarily providing opinions on the agencies' internal control; but most do not. When an auditor renders an opinion on internal control, the auditor is providing reasonable assurance that the entity has maintained effective internal control over financial reporting (including safeguarding of assets) and compliance such that material misstatements, losses, or noncompliance that are material to the financial statements would be detected in a timely fashion. For fiscal year 2002, however, only 3 of the 24 CFO Act agencies received opinions on internal control from their auditors.<sup>4</sup> The remaining 21 reported on internal control, but provided no opinion on the effectiveness of the agency's internal control. As we move closer to being able to issue an opinion on the consolidated financial statements, a disparity in reporting on internal control would hinder our ability to provide an opinion on internal control for the consolidated audit. Current agency-level reporting on internal control would fall short of what the public should be able to expect from an audit and, moreover, what is now legally required from the auditors of publicly traded companies.

Congress has prescribed auditor opinions on internal controls for publicly traded corporations under the Sarbanes-Oxley Act of 2002.<sup>5</sup> A final rule issued by the Securities and Exchange Commission in June 2003 and effective August 2003 provides guidance for implementation of section 404 of the act, which contains requirements for management and auditor reporting on internal controls. The final rule requires companies to obtain a report in which a registered public accounting firm expresses an opinion, or states that an opinion cannot be expressed, concerning management's assessment of the effectiveness of internal controls over financial reporting.

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<sup>4</sup>The three agencies receiving opinions on internal control for fiscal year 2002 are the Social Security Administration, General Services Administration, and Nuclear Regulatory Commission.

<sup>5</sup>Pub. L. No. 107-204, 116 Stat. 745 (2002).

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As you know, Mr. Chairman, we provided testimony before this Subcommittee several weeks ago on the challenges of establishing sound financial management within DHS.<sup>6</sup> In that testimony, we supported provisions of H.R. 2886 that would require DHS to obtain an audit opinion on its internal controls. During the testimony, we also supported provisions of H.R. 2886 that would require the Chief Financial Officers Council and the PCIE to jointly study the potential costs and benefits of requiring CFO Act agencies to obtain audit opinions of their internal controls over financial reporting. In addition, the current version of H.R. 2886 would require GAO to perform an analysis of the information provided in the report and report the findings to the House Committee on Government Reform and the Senate Committee on Governmental Affairs. We believe that the study and related analysis are important first steps in resolving the issues associated with the current reporting on internal control.

Ultimately, we are hopeful that federal performance and accountability professionals will not settle for anything less than opinion-level work on internal control at the CFO Act agency level and on the governmentwide audit. Increased planning and coordination will be needed among GAO, IGs, and IPAs to determine the appropriate timing for requiring an opinion on controls at the agency level. The specific timing will depend on the current state of the agency's control efforts so that an audit opinion on internal control would add value and mitigate risk in a cost beneficial manner.

A practical issue that should also be dealt with is the adequacy of resources to provide for the agency financial statement audits. Over the years, a number of IGs have told us that the cost of agency financial audits has taken resources away from their traditional work. In the private sector, the cost of an annual financial audit is a routine business expense borne by the entity being audited, and the cost of the audit represents a very small percentage of total expenditures for the audited entity. We support enacting legislation that would make agencies responsible for paying the cost of their financial statement audits. We also believe that an arrangement in which the agencies pay for their own audits provides them with positive incentives for taking actions—such as streamlining systems and cleaning up their financial records prior to the audit—in order to reduce the costs of

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<sup>6</sup>U.S. General Accounting Office, *Department of Homeland Security: Challenges and Steps in Establishing Sound Financial Management*, [GAO-03-1134T](#) (Washington, D.C.: Sept. 10, 2003).

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the audit and avoid the “heroic” audit efforts that we have seen in the past at some agencies.

Under the arrangement in which agencies pay the cost of their own audits, we believe the IG should continue in the current role of selecting and overseeing audits in those cases in which the IG does not perform the audit but hires an IPA to conduct the audit. This would leverage the IGs’ expertise to help assure the quality of the audits. We also advocate an approach whereby the IGs would be required to consult with the Comptroller General during the IPA selection process to obtain input from the results of GAO’s reviews of the IPAs’ previous work and the potential impact on the consolidated audit.

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## The IG Role in Federal Financial Management Advisory Committees

We envision an important role for the IGs in audit or financial management advisory committees established at the federal agency level for the purpose of overseeing an agency’s financial management, audits, and performance.

In the government arena, some state and local governments and federal government corporations, as well as several federal agencies, have adopted an audit committee, or “financial management advisory committee,” approach to governance. In the federal government, such audit committees or advisory committees are intended to protect the public interest by promoting and facilitating effective accountability and financial management by providing independent, objective, and experienced advice and counsel, including oversight of audit and internal control issues. Responsibilities of the committees would likely include communicating with the auditors about the audit and any related issues. The work of the IGs logically provides much of the basis for financial management advisory committees in overseeing agencies’ financial management, audits, and internal control. The work of the IGs would also be critical for the financial management advisory committees in their general governance roles. Specific roles and responsibilities of the committees will most likely vary by agency. A recently published guide, *Financial Management Advisory Committees for Federal Agencies*,<sup>7</sup> provides a helpful road map of suggested practices for federal agency financial management advisory committees.

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<sup>7</sup>*Financial Management Advisory Committees for Federal Agencies: Suggested Practices*, March 2003, prepared by KPMG, LLP.

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The concept of financial management advisory committees is very similar to the audit committee structure being used in the private sector. To help facilitate the audit process and promote disclosure and transparency, the governing boards of publicly traded companies use audit committees. Audit committees generally oversee the independent audit of the organization's financial statements and address financial management, reporting, and internal control issues. The Sarbanes-Oxley Act has requirements for the audit committees of publicly traded companies and their auditors regarding communications and resolution of significant audit matters.

We strongly support the implementation of financial management advisory committees for selected federal agencies, based on risk and value added. Some agencies,<sup>8</sup> including GAO, which has had such a committee in place since 1995, have already implemented such an approach, even though the committees have not been mandated or established by statute. As these committees are implemented or required in government, we would advocate amending the IG Act to emphasize the IGs' unique role in reporting the results of their work to the advisory committees while maintaining their independence and dual reporting authority to Congress.

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## Structural Streamlining to Increase Resource Efficiencies

One of the issues facing the IG community as well as others in the performance and accountability community is how to use limited resources to the best effect. In fiscal year 2002, the 57 IG offices operated with total fiscal year budgets of about \$1.6 billion and about 11,000 staff. (See app. II for more detail on IG budgets and staffs.) Most IGs for cabinet departments and major agencies are appointed by the President and confirmed by the Senate; however, IGs for some agencies are appointed by the agency head, and these IGs generally have smaller budgets and fewer staff than IGs appointed by the President. While agency-appointed IGs make up about half of all IG offices, the total of their fiscal year 2002 budgets was \$162.2 million, a little more than 10 percent of all IG budgets. Of these IGs, the offices at the U.S. Postal Service (USPS), Amtrak, National Science Foundation (NSF), and Federal Reserve Board (FRB) are exceptions and have budgets that are comparable in size to those of presidentially appointed IGs. The remaining 24 agency-appointed IGs have a total of 191

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<sup>8</sup>Agencies that currently have audit committees or financial management advisory committees include the National Science Foundation, Federal Deposit Insurance Corporation, and the Architect of the Capitol.

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staff and have budgets that make up about 2 percent of all IG budgets. Importantly, 16 of the 28 agency-appointed IGs have fewer than 10 staff.

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## Potential IG Office Consolidations

Last year we reported the views of the IGs, as well as our own, on the possible benefits of consolidating the smallest IG offices with the offices of IGs appointed by the President.<sup>9</sup> We also considered the conversion of agency-appointed IGs to presidential appointment where their budgets were comparable to the presidentially appointed IG offices. The August 2002 report contains several matters for congressional consideration to address issues of IG conversion and consolidation. We are reaffirming these views, which are included at the end of my statement.

We believe that if properly structured and implemented, the conversion or consolidation of IG offices could increase the overall independence, efficiency, and effectiveness of the IG community. Consolidation could provide for a more effective and efficient allocation of IG resources across government to address high-risk and priority areas. It would not only achieve potential economies of scale but also provide a critical mass of skills, particularly given advancing technology and the ever-increasing need for technical staff with specialized skills. This point is especially appropriate to the 12 IG offices with five or fewer staff. IG staff now in smaller offices would, in a large, consolidated IG office, have immediate access to a broader range of resources to use in dealing with issues requiring technical expertise or areas of critical need.

Consolidation would also strengthen the ability of IGs to improve the allocation of human capital and scarce financial resources within their offices and to attract and retain a workforce with talents, multidisciplinary knowledge, and up-to-date skills to ensure that each IG office is equipped to achieve its mission. Consolidation would also increase the ability of larger IG offices to provide methods and systems of quality control in the smaller agencies.

We also recognize that there are potential risks resulting from consolidation that would have to be mitigated through proactive and targeted actions in order for the benefits of consolidation to be realized without adversely affecting the audit coverage of small agencies. For

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<sup>9</sup>U.S. General Accounting Office, *Inspectors General: Office Consolidation and Related Issues*, GAO-02-575 (Washington, D.C.: August 2002).

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example, the potential lack of day-to-day contact between the IG and officials at smaller agencies as a result of consolidation could be mitigated by posting IG staff at the agency to keep both the IG and the agency head informed and to coordinate necessary meetings. In preparation for consolidation, staff in the smaller IG offices could be consulted in planning oversight procedures and audit coverage for their agencies. There may be fewer audits or even less coverage of those issues currently audited by the IGs at smaller agencies, but coverage by a consolidated IG could address areas of higher risk, value, and priority, resulting in potentially more efficient and effective use of IG resources across the government.

Results of the survey conducted for our August 2002 report indicate a clear delineation between the responses of the presidentially appointed IGs and the responses of the agency-appointed IGs. The presidentially appointed IGs generally indicated that agency-appointed IG independence, quality, and use of resources could be strengthened by conversion and consolidation. The agency-appointed IGs indicated that there would either be no impact or that these elements could be weakened. The difference in views is not surprising given the difference in the potential impact of consolidation on the interests of the two groups of IGs. We believe that this difference in perspective, more than any other factor, helps to explain the significant divergence in the responses to the survey.

There are already some examples where consolidation of IG offices and oversight is working. The Department of State IG provides, through statute, oversight of the Broadcasting Board of Governors and the International Broadcasting Bureau. The IG at the Agency for International Development is authorized by specific statutes to provide oversight of the Overseas Private Investment Corporation, the Inter-American Foundation, and the African Development Foundation.

In terms of budget size, the agency-appointed IGs at USPS, Amtrak, NSF, and FRB are comparable to the offices of IGs appointed by the President. Moreover, in the case of the Postal IG, the office is the fourth largest of all the IGs. (See app. II.) On that basis, these IGs could be considered for conversion to appointment by the President with Senate confirmation. While the Amtrak IG could be converted because of comparable budget size, oversight of Amtrak is closely related to the work of the Department of Transportation IG. Moreover, the Transportation IG currently provides some oversight of Amtrak programs. Therefore, the consolidation of the Amtrak IG with the Transportation IG could be considered, rather than conversion.



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Consideration has been given in the *Fiscal Year 2004 Budget of the U.S. Government* to the consolidation of the two IG offices at the Department of the Treasury, unique in the federal government. The original statutory IG for the Department of the Treasury was established by the IG Act amendments of 1988. The Treasury IG for Tax Administration was established in 1998 as part of an Internal Revenue Service (IRS) reorganization because the former IRS Inspection Service was not perceived as being sufficiently independent from management. Consequently, the IRS Office of the Chief Inspector, along with most of the Inspection Service staff, was transferred to the new IG office to ensure independent reviews.

The separate office of Treasury IG for Tax Administration was created because IRS officials were concerned that if the resources of the IRS Inspection Service were transferred to the original Treasury IG office, they would be used to investigate or audit other Treasury bureaus to the detriment of critical IRS oversight. With the passage of the Homeland Security Act of 2002, and the transfer of Treasury's United States Customs Service and United States Secret Service to the new Department of Homeland Security, the original concerns about competition for resources within the department should no longer be as compelling.

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## IG Councils

The PCIE is an interagency council comprising principally the presidentially appointed and Senate-confirmed IGs. It was established by Executive Order No.12301 in 1981 to coordinate and enhance the work of the IGs. In 1992, Executive Order No.12805 created the ECIE, which comprises primarily statutory IGs appointed by the heads of designated federal entities as defined in the IG Act. The Deputy Director for Management in OMB serves as the chair of both organizations. These IG councils have been effective in coordinating the activities of the IGs in their efforts to prevent and detect fraud, waste, and abuse throughout the federal government and in reporting these results to both the President and Congress.

The IG councils have provided a valuable forum for auditor coordination. However, we believe that the current environment demands a more formal, action-oriented, and strategic approach for coordination among federal audit organizations and that the IG councils could be strengthened in a number of ways. First, by providing a statutory basis for their roles and responsibilities, the permanence of the councils could be established and their ability to take on more sensitive issues strengthened. In addition, the

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strategic focus of the councils could be clearly established. As such, the councils would also be key in the overall strategic planning process for federal audit oversight that I described earlier in this statement.

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## Matters for Congressional Consideration

As I stated at the beginning of my testimony, IGs have made a significant difference in federal performance and accountability during the last quarter century. The 25th anniversary of the landmark legislation establishing the IGs is an opportune time to reflect on the IGs' success while also considering ways to enhance coordination and utilization of resources across the federal performance and accountability community.

In order to enhance the effectiveness and impact of the federal accountability community, Congress may want to consider establishing, through statute, assignment of responsibility to a selected group of designated federal accountability officials, such as representatives from GAO, the PCIE, and the ECIE, to develop and implement a periodic, formal strategic planning and ongoing engagement coordination process for focusing GAO and IG work to provide oversight to high-risk areas and significant management challenges across government, while leveraging each other's work and minimizing duplication.

In order to resolve resource issues and provide positive incentives to agencies to take prudent actions to reduce overall audit costs, Congress may want to consider enacting legislation that makes agencies responsible for paying the cost of their financial statement audits.

In order to achieve potential efficiencies and increased effectiveness across the federal IG community, Congress may also want to consider whether to proceed with a restructuring of the IG community, which could include the following:

- amending the IG Act to elevate the IGs at USPS, NSF, and FRB to presidential status,
- amending the IG Act to consolidate agency-appointed IGs with presidentially appointed IGs based on related agency missions or where potential benefits to IG effectiveness can be shown, and
- establishing an IG council by statute that includes stated roles and responsibilities and designated funding sources.

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Mr. Chairman, that concludes my prepared statement. I would be happy to respond to any questions you or Members of the Subcommittee might have.

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# The Inspector General Act

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The Inspector General Act of 1978 was enacted following a series of events that emphasized the need for more-independent and coordinated audits and investigations in federal departments and agencies. First, in 1974, the Secretary of Agriculture abolished the department's administratively established IG office, demonstrating the impermanent nature of a nonstatutory IG. Later, in 1974 and 1975, a study by the Intergovernmental Relations and Human Resources Subcommittee of the House Government Operations Committee disclosed inadequacies in the internal audit and investigative procedures in the Department of Health, Education, and Welfare, now the Department of Health and Human Services. The need to deal more effectively with the danger of loss from fraud and abuse in the department's programs led to the establishment of the first statutory IG in 1976. The Congress also established an IG in the Department of Energy when that department was created in 1977.

In 1977, the House Intergovernmental Relations and Human Resources Subcommittee began a comprehensive inquiry to determine whether other federal departments and agencies had a similar need for statutory IGs. The Subcommittee's study revealed serious deficiencies in a number of department and agency audit and investigative efforts, including the following:

- No central leadership of auditors and investigators existed.
- Auditors and investigators exhibited a lack of independence by reporting to officials who had responsibility for programs that were being audited.
- No procedures had been established to ensure that the Congress was informed of serious problems.
- No program existed to look for possible fraud or abuse.

As an initial effort to correct these deficiencies, the IG Act of 1978 established 12 additional statutory OIGs to be patterned after the one at the Department of Health, Education, and Welfare. The act consolidated the audit and investigative responsibilities of each department and agency under the direction of one senior official—the Inspector General—who reports to the head of the agency or, if delegated, the official next in rank below the agency head. The President appoints the IGs, by and with the consent of the Senate, without regard to political affiliation and solely on the basis of integrity and demonstrated ability in accounting, financial

analysis, law, management analysis, public administration, or investigations.

The IGs are responsible for (1) conducting and supervising audits and investigations, (2) providing leadership and coordination and recommending policies to promote economy, efficiency, and effectiveness, and (3) detecting fraud and abuse in their agencies' programs and operations. In addition, the IG Act requires IGs to prepare semiannual reports which summarize the activities of the IG during the preceding 6-month period. The reports are forwarded to the department or agency head, who is responsible for transmitting them to the appropriate congressional committees.

The act states that neither the agency head nor the official next in rank shall prevent or prohibit the IG from initiating, carrying out, or completing any audit or investigation, or from issuing any subpoena during the course of any audit or investigation. This enhances the independence of auditors and investigators by ensuring that they are free to carry out their work unobstructed by agency officials. The act further enhances independence by requiring IGs to comply with the Comptroller General's *Government Auditing Standards*. One of these standards requires auditors and audit organizations to be personally and organizationally independent and to maintain the appearance of independence so that opinions, conclusions, judgments, and recommendations will be impartial and will be viewed as such by knowledgeable third parties.

Between the enactment of the IG Act in 1978 and 1988, the Congress passed legislation to establish statutory IGs, who are appointed by the President with Senate confirmation, in 8 additional departments and agencies. In 1988, the Congress enacted the Inspector General Act Amendments of 1988 and the Government Printing Office (GPO) Inspector General Act of 1988 (Titles I and II, Public Law 100-504) to establish additional presidentially appointed IGs in 5 departments and agencies and 34 IGs appointed by their agency heads (33 in designated federal entities and 1 in GPO) in order to strengthen the capability of the existing internal audit offices and improve audit oversight. Both GAO and the President's Council on Integrity and Efficiency (PCIE) had previously reported that the existing internal audit offices lacked independence, adequate coverage of important programs, and permanent investigative staff.

# Inspector General Budgets and Staffing

**Table 1: Inspectors General Appointed by the President, Fiscal Year 2002 Budgets and Full-Time Equivalents (FTEs)**

Federal departments/agencies		Budgets	FTEs
1	Department of Health and Human Services <sup>a</sup>	\$227,000,000	1,569
2	Department of Defense	151,000,000	1,215
3	Treasury IG for Tax Administration	130,000,000	943
4	Department of Housing and Urban Development	95,000,000	648
5	Social Security Administration	75,000,000	564
6	Department of Agriculture	75,000,000	642
7	Department of Labor	67,000,000	426
8	Department of Justice	65,000,000	329
9	Department of Veterans Affairs	57,000,000	393
10	Department of Transportation	50,000,000	454
11	Department of Homeland Security	47,000,000	336
12	Environmental Protection Agency	46,000,000	444
13	Department of Education	39,000,000	276
14	Department of the Interior	37,000,000	251
15	General Services Administration	36,000,000	273
16	Department of Energy	32,000,000	250
17	Agency for International Development	32,000,000	166
18	Federal Deposit Insurance Corporation	32,000,000	201
19	Department of State	29,000,000	234
20	National Aeronautics and Space Administration	24,000,000	200
21	Department of Commerce	21,000,000	136
22	Small Business Administration	12,000,000	108
23	Department of the Treasury	12,000,000	87
24	Office of Personnel Management	11,000,000	89
25	Tennessee Valley Authority	7,000,000	87
26	Nuclear Regulatory Commission	6,000,000	41
27	Railroad Retirement Board	6,000,000	51
28	Corporation for National and Community Service	5,000,000	16
29	Central Intelligence Agency <sup>b</sup>	na	na
<b>Total</b>		<b>\$1,426,000,000</b>	<b>10,429</b>

Source: Budget authority and FTEs from *Fiscal Year 2004 Budget of the U.S. Government*.

<sup>a</sup>Includes budget authority to combat health care fraud.

<sup>b</sup>Budget and FTE information not available.

**Appendix II**  
**Inspector General Budgets and Staffing**

**Table 2: Inspectors General Appointed by Agency Heads, Fiscal Year 2002 Budgets and Full-Time Equivalents (FTEs)**

<b>Federal agencies</b>		<b>Budgets</b>	<b>FTEs</b>
1	U.S. Postal Service	\$117,324,000	713
2	Amtrak	8,706,539	64
3	National Science Foundation	6,760,000	50
4	Federal Reserve Board	3,878,000	29
5	Government Printing Office	3,400,000	24
6	Legal Services Corporation	2,500,000	15
7	Peace Corps	2,006,000	16
8	Smithsonian Institution	1,800,000	17
9	Federal Communications Commission	1,569,000	10
10	National Archives and Records Administration	1,375,000	13
11	Securities and Exchange Commission	1,372,559	8
12	National Credit Union Administration	1,338,135	7
13	Pension Benefit Guaranty Corporation	1,300,000	11
14	Equal Employment Opportunity Commission	1,106,119	10
15	Federal Housing Finance Board	858,237	3
16	Farm Credit Administration	829,621	5
17	Commodity Futures Trading Commission	735,800	4
18	Corporation for Public Broadcasting	735,000	9
19	National Labor Relations Board	711,900	6
20	Federal Trade Commission	710,000	5
21	National Endowment for the Humanities	497,000	5
22	Appalachian Regional Commission	466,000	3
23	Federal Maritime Commission	441,034	3
24	Consumer Product Safety Commission	407,000	3
25	Federal Election Commission	392,600	4
26	National Endowment for the Arts	392,577	4
27	International Trade Commission	389,500	4
28	Federal Labor Relations Authority	222,500	2
<b>Total</b>		<b>\$162,224,121</b>	<b>1,047</b>

Source: As reported by the ECIE.

**Appendix II**  
**Inspector General Budgets and Staffing**

**Table 3: Inspectors General Appointed by the President with Four Comparable Agency-Appointed IGs Fiscal Year 2002 Budgets**

<b>Department/agency IG</b>		<b>Fiscal year 2002 budgets</b>
1	Department of Health and Human Services <sup>a</sup>	\$227,000,000
2	Department of Defense	151,000,000
3	Treasury's IG for Tax Administration	130,000,000
4	<b>U.S. Postal Service<sup>b</sup></b>	117,324,000
5	Department of Housing and Urban Development	95,000,000
6	Department of Agriculture	75,000,000
7	Social Security Administration	75,000,000
8	Department of Labor	67,000,000
9	Department of Justice	65,000,000
10	Department of Veterans Affairs	57,000,000
11	Department of Transportation	50,000,000
12	Department of Homeland Security	47,000,000
13	Environmental Protection Agency	46,000,000
14	Department of Education	39,000,000
15	Department of the Interior	37,000,000
16	General Services Administration	36,000,000
17	Department of Energy	32,000,000
18	Agency for International Development	32,000,000
19	Federal Deposit Insurance Corporation	32,000,000
20	Department of State	29,000,000
21	National Aeronautics and Space Administration	24,000,000
22	Department of Commerce	21,000,000
23	Department of the Treasury	12,000,000
24	Small Business Administration	12,000,000
25	Office of Personnel Management	11,000,000
26	<b>Amtrak<sup>b</sup></b>	8,706,539
27	Tennessee Valley Authority	7,000,000
28	<b>National Science Foundation<sup>b</sup></b>	6,760,000
29	Nuclear Regulatory Commission	6,000,000
30	Railroad Retirement Board	6,000,000
31	Corporation for National and Community Service	5,000,000
32	<b>Federal Reserve Board<sup>b</sup></b>	3,878,000
33	Central Intelligence Agency <sup>c</sup>	na
<b>Total</b>		<b>\$1,562,668,539</b>

Source: Budget authority from Fiscal Year 2004 Budget of the U.S. Government.



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**Appendix II**  
**Inspector General Budgets and Staffing**

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Note: The four comparable agency appointed IGs are in bold.

<sup>a</sup>Includes budget authority to combat health care fraud.

<sup>b</sup>Information supplied by the ECIE.

<sup>c</sup>Budget information not available.

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