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# Government Management—Report on 17 High-Risk Areas

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Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss our high-risk series of reports--the second series of special reports we have released this week. The series focuses on the federal government's efforts to identify and correct problems in 17 areas that we identified as especially vulnerable to waste, fraud, abuse, and mismanagement. It summarizes the results of congressional, federal agency, and our efforts over the 3 years since we announced the implementation of our high-risk program before this Committee. I would like to commend you, Mr. Chairman, and the members of this Committee for your continued support and efforts in helping to strengthen federal programs and in helping us make this effort a success.

In my testimony on our transition series, I pointed out that the state of management in the federal government is not good. Too many principles, structures, and processes that may have worked well years ago no longer allow the government to respond quickly and effectively to a rapidly changing world.

For too long, progress in changing this situation has been slow. Incremental improvements have occurred. But time and again over the past decade, our management reviews of large federal agencies and departments have shown that the processes and systems fundamental to a well-run organization are often not present. Most agencies have not created a strategic vision for the future, most lack good systems to collect and use financial and program information to gauge operational success and accountability, and many do not have people with the necessary skills to accomplish their missions.

These elements are essential for any organization to succeed. But they usually do not command the attention of senior political officials coming into the government. After all, these elements do not appear to be directly related to the development of an administration's policies or programs and, therefore, do not seem important to achieve a political agenda. However, many of our audit reports demonstrate the effects of leaders' inattention to these elements--waste, inefficiency, and even scandal. Political leaders then have to spend too much time and energy reacting to surprises resulting from management failures rather than pursuing the mission of their agencies and their policy agenda.

We started our high-risk program to identify those high dollar programs that are particularly vulnerable to fraud, waste, abuse, and mismanagement. These programs involve tens of billions of dollars. Our focus was on finding the root causes of program vulnerabilities and on directing management attention to these issues.

As you will hear this morning, many of the causes go back to the lack of fundamental processes and systems. Correcting the problems will require a long-term effort and top management attention and support. We are recommending that the Congress provide the necessary focus and attention by conducting annual oversight hearings. Among other things, this oversight process should focus on the reports and audited financial statements required by the Chief Financial Officers Act, agency management's progress in correcting material weaknesses in program internal control and accounting systems, and federal agency efforts to develop and implement performance standards against which their efficiency and effectiveness can be measured.

## THE GOVERNMENT HAS A HISTORY OF INEFFICIENT AND INEFFECTIVE PROGRAM MANAGEMENT

The Department of Housing and Urban Development (HUD) scandal of 1989 rocked the government and further shattered taxpayer confidence in the government's ability to effectively manage its programs and safeguard and account for program assets. After 3 years and despite publicity and actions by the Congress and top-level agency officials, HUD is still vulnerable to major losses. In fact, a recent inspector general report cautions that "despite all of these collective efforts and momentum in reforming Departmental programs and operations, another HUD scandal is a distinct possibility unless the Department has sufficient resources to carry out its formidable mandate."

I believe the HUD scandal of the 1980s is an example of what can go wrong when management disregards its responsibilities and other oversight mechanisms do not work as expected. However, history shows that pervasive problems that cost the taxpayer billions of dollars exist across the spectrum of federal activities and that federal efforts to eliminate these problems, including legislative mandates, have generally fallen short of their expectations.

For example, the Congress passed the Federal Managers' Financial Integrity Act in September 1982 in an attempt to strengthen internal control and accounting systems throughout the federal government and to reduce fraud, waste, abuse, and misappropriation of federal funds. This legislation requires all executive agencies to prepare annual reports to the President and the Congress on the condition of internal control and accounting systems throughout their organizations. During the next 10 years, federal agencies identified thousands of material internal control weaknesses and developed and implemented plans to correct these weaknesses. However, new problems continue to emerge and overall progress, in my judgement, has been slight.

When we started our high-risk program in November 1989, we reported that the government's efforts to strengthen its programs and implement the Financial Integrity Act had not produced the results intended by the Congress. It was evident that

-- the government did not have the internal control and accounting systems necessary to effectively operate many of its programs and safeguard its assets;

-- many of the weaknesses were long-standing and had resulted in billions of dollars of losses and wasteful spending;

-- the public perceived the federal government to be poorly managed, with little or no control over its activities; and

-- top-level officials needed to provide leadership if this situation was to ever change.

The situation is much the same today. Our high-risk series of reports focuses on the fundamental causes of existing problems; progress made in correcting them; and actions the Congress, the administration, and agency officials need to take to ensure more efficient and effective program operation. In many cases, major problems persist and the danger remains for losses of billions of dollars. These reports also show that progress has begun in some cases and that, in limited areas, really significant progress has been made. For example, when the Federal Deposit Insurance Corporation Improvement Act, passed in December 1991, is fully implemented, it will help correct fundamental weaknesses in the deposit insurance system by addressing accounting, corporate governance, and regulatory problems.

## IMPLEMENTATION OF OUR HIGH-RISK PROGRAM

Despite our hopes that the Financial Integrity Act would be successfully implemented and that agencies would act on recommendations in inspector general and our audit reports to strengthen their programs, we had to face reality. Agency problems were not getting fixed. To address this situation, we and the Office of Management and Budget (OMB) initiated more focused efforts to bring greater attention to selected areas and to the government's actions to correct problems within those areas.

To do this, we developed a high-risk program with three purposes. First, based on our audit experience and the magnitude of potential dollar losses, we wanted to identify areas highly vulnerable to fraud, waste, abuse, and mismanagement. Second, in concert with the agencies and the inspectors general, we wanted to identify actions to correct the problems. Finally, we wanted to conduct in-depth audits and undertake an ongoing monitoring of the high-risk areas to include a review of progress reports; followup with agency personnel; and notification of the Congress when corrective actions appeared to be ineffective, ran seriously behind schedule, needed to be revised significantly, or required additional resources to be carried out effectively and expeditiously.

OMB's high-risk program encompasses many more areas than ours--106 initially in 1989 and 99 in January 1992. This program provides a much needed focus and emphasis by top level officials in federal agencies. Although OMB staff limitations have prevented intensive concentration on the problems, there have been some successes. Focus on high-risk areas in the President's budget has also helped.

SUMMARY FINDINGS IN HIGH-RISK AREAS

For discussion purposes, we have categorized our 17 high-risk areas into three general issue areas--lending and insuring, contracting, and accountability. It is important to mention at this point that correcting the problems requires not only fixing agency internal control systems but also improving federal oversight of nonfederal organizations, including defense contractors and banks and other financial institutions. Experience has shown that these organizations often suffer weak internal controls.

Lending and Insuring Issues

The federal government is a major insurer, lender, and guarantor through a wide range of programs designed to provide opportunities for personal and business advancement and to help safeguard certain assets. Poor program oversight and structural inefficiencies, reliance on others to perform key program activities, the lack of financial and other management controls, and congressionally imposed constraints combine to make these programs highly vulnerable to fraud, waste, abuse, and mismanagement. Furthermore, these factors have caused billions of dollars in losses and threaten added losses if problems are not corrected.

The following six areas fall into this category:

-- Farmers Home Administration's Farm Loan Programs,

-- Guaranteed Student Loans,

-- the Bank Insurance Fund,

-- the Resolution Trust Corporation,

-- the Pension Benefit Guaranty Corporation, and

-- Medicare claims.

The Farmers Home Administration's (FmHA) Farm Loan and the Guaranteed Student Loan (GSL) programs have incurred billions of dollars of loan losses.

Farmers Home Administration's Farm Loan Programs. Marred by high default rates, FmHA's loan program has reduced or forgiven delinquent debt totaling about $7.6 billion in recent years. FmHA and the Congress share responsibility for many of FmHA's problems. Although some contributing factors--such as the general decline of the agricultural economy in the 1980s--have been beyond the control of FmHA or the Congress, two major factors do lie within their authority. First, FmHA field office lending officials often fail to follow the agency's own standards for making loans, servicing loans, and managing property. Second, FmHA loan-management and property-management policies--some of which are congressionally directed--do not adequately protect taxpayers' interests. For example, these policies allow borrowers who have defaulted on past FmHA loans to obtain new ones.

Guaranteed Student Loans. While the GSL program has generally succeeded in providing access to money for education, it has been less successful in protecting taxpayers' financial interests. In 1991, the federal government paid out $3.6 billion to make good its guarantee on defaulted student loans, thus continuing a trend of escalating losses.

These losses were caused by several factors. First, fundamental problems exist in the student loan program's structure and management. In part, these stem from the tension between the conflicting goals of providing steadily increasing loan funds so that students can meet rising education costs and of minimizing costs to taxpayers. Over the years, the Congress and the Department of Education have tended to emphasize access to loans at the expense of protecting taxpayer interests. Many schools, lenders, and guaranty agencies have little or no incentive to prevent defaults. Each type of entity benefits from the loans that are made but generally bears no financial risk. Nearly all risk falls to the federal government, whose only recourse is to pursue recovery from student borrowers. Second, the Department of Education has failed to weed out some schools that collect tuition payments and provide marginal instruction. Finally, Education's records had been inaccurate and incomplete, it had conducted little oversight of lenders and guaranty agencies, and it had inadequately trained and organized program staff.

Bank Insurance Fund. Because of an upsurge in bank failures, the Bank Insurance Fund lost more than $25 billion in 4 years. As of December 1991, the Fund was $7 billion in the red. Between 1987 and 1991, 882 banks with assets totaling $151 billion failed.

Weak internal controls, flawed corporate governance systems, and lax regulatory supervision put both the banks and the Fund at risk. Meanwhile, flexible accounting standards contributed to the problem by enabling weak institutions to hide the extent of their problems while their losses grew. Even while costs to the Fund mounted, neither the Congress nor the administration received an early warning of the size of the problem from the federal budgetary system. Under current cash-based budget practices, costs to the deposit insurance system are already incurred by the time their impact on the budget is recognized.

The Federal Deposit Insurance Corporation Improvement Act, enacted in December 1991, contains accounting, corporate governance, and regulatory reforms--which we strongly supported--designed to correct weaknesses in the deposit insurance system. Among other measures, the act's reforms provide for the timely disclosure of internal control weaknesses and violations of laws and regulations, independent audit committees, and capital and safety and soundness standards. These requirements are designed to strengthen corporate governance and to ensure that regulators take prompt and appropriate actions to correct unsafe banking practices and minimize losses to the Fund.

Resolution Trust Corporation. The Resolution Trust Corporation (RTC) has received widespread publicity since its inception a few years ago. It has discharged some of its resolution and asset sales responsibilities fairly well. However, poor planning and execution of real estate disposition strategies, problems with the contracting system, and inadequate information systems have hampered its overall performance. Deficiencies in these areas reduce the amount of money RTC recovers through asset disposition and increase the likelihood that taxpayers will need to cover additional costs.

Two of the factors contributing to RTC's problems are outside of its control. The first is the sheer amount of taxpayer funds involved in the program due to the losses associated with failed thrifts. The second is the country's economic environment in which, during the past 3 years, the demand for whole thrifts has been limited, real estate markets have declined, the availability of credit to finance asset purchases has been uncertain, and the economy as a whole has been in recession. At the same time, RTC's inventory is becoming increasingly concentrated in assets in hard to sell categories.

However, RTC has experienced significant problems in handling matters within its control, including its approaches to asset disposition, its contracting system, and its asset information systems. For example, RTC has used inefficient and inadequately planned sales approaches; does not adequately define needed services, the scope of work, and the types of contracts that could best accomplish these ends; and has difficulty overseeing the tens of thousands of contractors who manage and dispose of billions of dollars in assets on its behalf. Further, RTC had not developed systems to provide the timely, accurate, and complete information needed to manage and evaluate disposition programs and oversee contractors. While RTC has taken steps to correct these problems, much work remains.

In addition to these problems, RTC's efforts have been hampered by repeated funding disruptions. RTC has run out of funds and has had to stop resolving thrifts three times since it was established. Until funds are provided, thrifts will continue to post millions of dollars in losses that will add to the overall cleanup costs.

Pension Benefit Guaranty Corporation. Another area that could result in billions of dollars in costs to the taxpayer is the Pension Benefit Guaranty Corporation (PBGC). Its problem is a large and growing unfunded deficit that threatens the insurance program's long-term financial viability. At the end of fiscal year 1991, this unfunded deficit--which had been accumulating since PBGC's inception in 1974--stood at an estimated $2.3 billion. By 2001, under PBGC's most pessimistic projection, the figure could reach $17.9 billion. Its financial condition has worsened because companies that have been allowed to underpay their plans have subsequently collapsed, thereby throwing the burden of paying employee benefits onto PBGC.

Two features in the design of the pension insurance program have made it hard for PBGC to control the risks it faces due to underfunded pension plans. First, the Employee Retirement Income Security Act's minimum funding standards do not ensure that pension plan sponsors will contribute enough so that, if the plans terminate, there will be sufficient assets to cover all the promised benefits. Second, the premiums that PBGC charges pension plans do not fully cover the risks that PBGC assumes.

In addition, PBGC has weaknesses in its internal control and financial systems. These weaknesses include the lack of a reliable method for estimating its liability for future benefits; serious problems with its premium reporting and collection system; and inadequate efforts to identify and collect delinquent premiums, underpaid premiums, and related interest and penalties. PBGC has been working to improve its internal control and financial systems, but our audit of its 1991 financial statements showed that they were not auditable. PBGC made additional progress in 1992, and we are currently auditing its 1992 financial statements.

Medicare Claims. In recent years, the Medicare program has lost billions of dollars to waste, fraud, and abuse. In 1991, the program enrolled about 35 million beneficiaries, processed about 600 million claims, and paid physicians and other providers over $110 billion in medical benefits--about 15 percent of all the money spent on health care in the United States. The Health Care Financing Administration (HCFA), which administers the Medicare program, relies on numerous contractors to process claims and to protect program funds through review activities called payment "safeguards." However, HCFA's inability to properly manage contractors' safeguard activities and too little money earmarked for these activities have left Medicare dollars exposed to loss and waste. For example, we found that contractors paid an estimated

$2 billion in claims that should have been paid by other health insurers. We also found that hospitals owed Medicare over $170 million in overpayments, but contractors had done little to recover the money. Moreover, HCFA was unaware of contractor inaction because it had no systems to monitor this information.

Medicare is also vulnerable to exploitation for other reasons. These include (1) payment policies that permit excessive reimbursement rates for certain services, such as high-tech and laboratory services, and (2) loose controls over who can bill Medicare, making the pursuit of fraudulent providers difficult.

Contracting Issues

The federal government spends hundreds of billions of dollars annually for contracted goods and services. Our high-risk areas under this category are

-- defense weapons systems acquisition,

-- defense contract pricing,

-- Department of Energy contract management,

-- Superfund program management, and

-- NASA contract management.

While agencies have recognized that management problems have existed in these areas for many years, the development and implementation of corrective actions has been slow at best and the effectiveness of these actions, disappointing. Although the missions, programs, and activities of the federal agencies in which these problems exist differ greatly, the problems share several common causes. These include inefficient oversight, inadequate data on contractor/provider operations, and contract provisions that restrict the government's ability to manage and control contractor activities and protect the government's interests.

Defense Weapons Systems Acquisition. The underlying cause of the persistent and fundamental problems in the Department of Defense's (DOD) weapons acquisition process is a culture that depends on generating and supporting new weapons acquisitions. This culture consists of the underlying assumptions, beliefs, values, attitudes, and expectations shared by the various components of DOD, the Congress, and industry. It provides powerful incentives and interests that influence and motivate the behaviors of these participants in the weapons acquisition process.

Despite many efforts to reform and improve DOD's weapons acquisition process over the years, a number of fundamental problems persist. All too often we have found the following types of problems.

-- The weapons systems acquired may not be the most cost-efficient solution to the mission need. While the military services perform considerable analyses to justify major acquisitions, these analyses can be narrowly focused exercises that do not fully consider alternative solutions. For example, in reviewing DOD's determination of weapons system requirements for its close support mission, we found that Air Force and Army analyses of alternatives to satisfy their mission needs were limited to specific types of weapons within their purview. The analyses gave little, if any, consideration to the contributions of other close support weapons, especially those from other service branches.

-- Overly optimistic weapons system cost and schedule estimates lead to program instability and cost increases. Cost growth and schedule delays, two of the most prevalent acquisition problems, are among the oldest and most visible problems associated with weapons systems. Because program sponsors want to keep cost estimates low and present attractive milestone schedules, they have used unreasonable assumptions about the pace and magnitude of the technical effort, material costs, production rates, savings from competition, and other factors. As a result, program cost increases on the order of 20 to 40 percent have become common for major weapons programs.

-- Programs cannot be executed as planned with available funds. DOD's spending plans for future years have assumed much higher funding levels than are actually obtained. As a result, program managers make development and production plans and schedules based on funding levels that ultimately are not realized. This leads to program reductions, delays, and/or stretchouts--adding millions of dollars to their costs. While DOD has made progress in this area in recent years, its spending plans still do not keep pace with the rapid changes in the national security environment.

-- Program acquisition strategies are unreasonable or risky at best. The acquisition strategy is a comprehensive plan of how to achieve the goals and objectives of the weapons system program and is a major determinant of program outcomes. However, the two most basic demands an acquisition strategy must meet--developing and fielding the weapon as quickly as possible to counter the threat and, at the same time, minimizing technical and cost risks--are inherently conflicting. For example, a strategy that optimizes accelerated fielding will likely accept higher risk primarily through concurrent development and production of the weapon system. Under such a strategy, major problems are more likely to be discovered in production, when it is either too late or very costly to correct them.

-- Too much is spent before a program is shown to be suitable for production and fielding. Many weapons encounter significant problems on the production line and in the field. Although DOD took steps during the 1980s to place increased emphasis on operational suitability considerations during the acquisition process, we continue to witness weapons systems that are deployed without reliable support and test equipment or with design problems that require retrofits and modifications to make them suitable for field use. The Apache helicopter and the Advanced Medium Range Air-to-Air missile are examples.

Culture is not the cause of all the problems in weapons acquisitions. Some problems can be attributed to basic errors in judgment or other motivating forces. For example, the big money involved in defense acquisitions can lead to influence-peddling and contracting fraud and abuse--as found in the "Ill Wind" investigation.

Defense Contract Pricing. In another area within DOD, contract overpricing remains a significant and widespread problem that costs taxpayers billions of dollars more than necessary for the goods and services purchased. While DOD has taken some steps to address contract overpricing problems, serious shortcomings remain. Specifically, (1) contractors' cost-estimating systems are often inadequate, (2) oversight by DOD is too little and too late, and (3) the application of monetary and other penalties is insufficient to change contractors' behavior in any meaningful way.

While the government is at risk for overpricing in prime contracts, it is particularly at risk in subcontracts. Subcontracts frequently account for more than 50 percent of a contract's costs. DOD relies heavily on the prime contractor and the quality of contractor cost-estimating systems to ensure reasonable subcontract prices.

Department of Energy Contract Management. Still other contracting problems arise because of the terms of government contracts. For example, the Department of Energy's (DOE) contracting approach (that is, its philosophy of "least interference" and mutuality clauses) has led to contracts that have virtually tied DOE's hands in terms of oversight. For example, they have required DOE to reimburse contractors for money and materials that the contractors' own employees have stolen and for fines that the contractors have incurred by violating environmental laws. DOE's inability to effectively oversee contractor operations has resulted in excessive subcontracting costs, missing classified documents, and funding of unauthorized projects.

Responding to calls for increased oversight, DOE has taken steps to reform its management philosophy and practices and to give contractors more incentive to act responsibly. DOE is realigning field and headquarters organizational relationships to build better accountability and has begun to revise contracts to strengthen contractor oversight. However, considering DOE's history of reliance on contractors, completing these changes will take time and a significant leadership effort.

Superfund Program Management. The Environmental Protection Agency's (EPA) Superfund program was created in 1980 as a short-term project to clean up the nation's worst hazardous waste sites. Although a definitive cost estimate for completing the cleanup effort has yet to be determined, it is clear that in the coming decades cleaning up thousands of Superfund sites, hundreds of which are owned by the federal government, could cost hundreds of billions of dollars.

Although it relies heavily on contractors to perform much of its cleanup work, EPA ignored long-standing deficiencies in the management of its contracts until this past year. More specifically, it failed to properly control contractors' costs or reduce Superfund's vulnerability to excessive damage claims resulting from contractors' negligence.

In addition, the federal government lacks an adequate system for assessing the health and environmental risks posed by Superfund sites relative to other environmental problems. Without this information, priorities cannot be set or resources allocated effectively. Further, EPA has recovered only a small fraction of the Superfund resources that it has spent. As of September 30, 1992, EPA had collected just 10 percent of the $5.7 billion that it had classified as recoverable from responsible parties. However, because it lacks complete data on its past recovery efforts, EPA cannot explain this low repayment rate. Also, although EPA has recently proposed regulations to change its approach to recovering indirect costs, so far it has excluded over $1 billion in prior costs from its recovery efforts. In addition, potential recoveries have been reduced by the Superfund law's restrictions on charging interest.

NASA Contract Management. The National Aeronautics and Space Administration's (NASA) procurement budget is one of the largest of all civilian agencies in the federal government. Since the late 1980s, NASA has acknowledged that its contract management is vulnerable to waste and mismanagement.

NASA's contract management difficulties have been largely linked to three major internal problems. First, its planning has not been realistic and has been based on a much higher level of funding than was likely to be made available. Since about 90 percent of NASA's funds are spent on contracts, adjusting to lower than expected funding levels often involves extending schedules, thereby increasing contract costs. Second, NASA has sometimes used ineffective procedures and systems to oversee and manage contractors. The lack of uniform testing policies and the inability to adequately oversee contractors' activities contributed to problems such as those affecting the GOES-Next weather satellites. Further, problems with cost reporting, property management, accounting, and information systems have impaired NASA's ability to monitor contracts. Finally, some of NASA's field centers have not been fully complying with governmentwide, agency, or field center contract management requirements, primarily because they were operating with ineffective guidance and oversight from NASA headquarters.

NASA's management has initiated several improvement efforts. Many of its initiatives are intended to help the agency regain control over the cost, schedule, and technical performance of contractors. In principle, we support NASA's initiatives and believe they offer the promise of eventual improvement in the agency's ability to adequately oversee its contractors. However, given the magnitude and longstanding nature of NASA's problems in contract management and related areas, its management faces a formidable challenge. The problems will not be corrected quickly and sustained effort will be required.

Accountability Issues

Both lending and insuring and contracting issues are affected by accountability problems. However, for another group of high-risk areas, accountability poses the primary problem they face. All have serious difficulties in obtaining and maintaining current and accurate information on program operations or activities. They lack accurate and timely financial and other information necessary to manage, and agency practices permit or condone inefficient and ineffective program operations. The areas in this category are

-- defense inventory management,

-- Internal Revenue Service receivables,

-- managing the Customs Service,

-- management of overseas property,

-- Federal Transit Administration grant management, and

-- asset forfeiture programs.

Defense Inventory Management. In the area of inventory management, DOD has wasted billions of dollars on excess supplies and spare parts (currently estimated at about $40 billion), burdened itself with the need to maintain them, and failed to acquire the tools or expertise to manage them effectively. These problems have been caused by DOD's traditional failure to stress the importance of proper inventory management or to provide its personnel with the needed tools and incentives to promote satisfactory performance. DOD uses inadequate data, fails to use new and more effective business techniques that would allow lower inventory levels, and believes that keeping large inventories is the way to ensure that it is always able to fill orders. Weaknesses in DOD inventory records, in-transit controls, computer systems, and physical security programs create rampant opportunities for theft and mismanagement.

DOD has recognized that changes to its business processes are essential. For example, the establishment of the Defense Business Operations Fund (DBOF) has helped focus DOD on the need to operate its support activities, such as supply operations, in a more business like manner. DBOF is aimed at charging the military units the full cost of services and supplies provided to them. Previously, military units received services and supplies either free of charge or at less than full cost. The practice of charging the military units full costs for services and supplies should help provide financial discipline and should also save money by providing the units with incentives to replace items only when necessary and by putting pressure on the supply system to introduce more efficient operations and drive the cost down as questions are raised about the cost of items.

Internal Revenue Service Receivables. The Internal Revenue Service (IRS) is responsible for routine tax collection and for pursuing delinquent payments. Although IRS routinely collects about a trillion dollars each year, its efforts to collect delinquent taxes have been inefficient and unbalanced. As a result, billions of dollars in taxes remain uncollected, representing a serious loss of revenue for the government.

Several problems have interfered with IRS's ability to collect unpaid taxes. IRS's records are inaccurate and insufficient; its collection process is lengthy, antiquated, rigid, and inefficient; it has had difficulty balancing collection efforts with the need to protect the taxpayer; its decentralized structure tends to blur lines of responsibility and accountability; and it does not have enough information to allocate staff effectively.

While IRS has begun to develop some much needed information on the accounts receivable inventory, taken a step toward establishing a unified collection strategy by appointing an accounts receivable executive officer, and included collection goals in its strategic planning process, many areas have yet to be addressed. These include gathering more and better data and removing organizational impediments to collections. Further, the Congress could revisit the issue of the appropriate balance between the need to protect taxpayers and the need to collect delinquent tax debts.

Managing the Customs Service. Another high-risk area, the Customs Service, cannot ensure that it is meeting its responsibilities to combat unfair foreign trade practices or protect the public from unsafe goods. It did not detect about 84 percent of the estimated trade law violations in imported cargo during fiscal year 1991. Also, the Customs financial management system does not provide reliable information on operating costs and the status of accounts receivable, lacks data integrity in the general ledger, makes contract payments without proof of delivery or acceptance of goods and services, and has weak internal controls over overtime payments to Customs inspectors.

Customs lacks an effective strategic management process to guide its operations and establish accountability for performance. Further, it is experiencing related weaknesses in information management, financial management, human resource management, performance management, and organizational structure. Left uncorrected, these weaknesses could hinder Customs' capacity to meet the challenges of the changing world trade environment.

## AGENCIES ARE TAKING ACTIONS TO ELIMINATE PROBLEMS

While the areas discussed so far have focused primarily on the management and programmatic problems facing many agencies, substantial strides in improving the conditions within some program areas have also occurred. In the past, agencies often either refused to recognize problems or argued that procedures in place ensured that the program(s) operated as intended. Now, however, some are more openly recognizing problems and are developing and implementing programs to eliminate them or mitigate their impact.

The following examples demonstrate some of this changed thinking and the corrective actions taken.

-- Until recently, the Federal Transit Administration (FTA) focused its resources on awarding grants rather than on ensuring their proper use. FTA's ineffective oversight of transit grants has enabled grant recipients to misuse millions of dollars in federal funds. Grant recipients' problems with financial management, procurement, and inventory control have gone undetected or uncorrected for as long as a decade or more. In the spring of 1992, FTA acknowledged the problems cited by us and by Transportation's inspector general and began implementing an oversight strategy. The success of this strategy will ultimately depend on the support that the administration and the Congress give to FTA's efforts to impose appropriate controls on grant recipients. If carried out in full, the new strategy should substantially improve grant recipients' compliance and better safeguard federal transit dollars.

-- At the Department of State, management of its overseas properties has been a chronic problem due to lax oversight, inadequate information systems, insufficient maintenance, and poor planning. After years of neglect and broken promises of action, State's Office of Foreign Buildings Operations has begun to correct some of its problems. It intends to establish priorities for construction projects based on specific criteria, to better evaluate contractors' performance, to hire additional qualified staff, to survey the maintenance conditions of posts worldwide, and to improve information systems. While these reforms offer promise, some key improvements are still in the initial stages and will take years to implement. It is important that State continue these efforts to make long-lasting improvements, especially in view of the increased work load and the demand for resources associated with opening new posts in the former Soviet Union.

-- In the asset forfeiture area, the Department of Justice, the Customs Service, and the Congress have taken actions to eliminate several major problems. The Congress established asset forfeiture funds at both agencies, into which proceeds from seizure activities are deposited and are used to finance program expenses. Previously, expenses were paid from agency appropriations for salaries and expenses, providing little incentive for the agencies to properly manage and maintain seized property. Further, Justice and Customs established policies to minimize delays in depositing seized cash and have established systems for overseeing seized cash operations. Finally, both agencies have made considerable progress in establishing systems to produce the reliable inventory data needed to make informed management decisions.

## SOME PROBLEMS IN HIGH-RISK AREAS PERVADE FEDERAL AGENCIES

Our transition series contains three crosscutting reports that bear directly on the problems in the 17 high-risk areas. Despite the wide differences between the types of programs in the high-risk areas, their intended goals and objectives, and their organization structures and methods of operation, they share several common problems. Foremost among these problems are financial management, information management, and general management deficiencies.

### Pervasive Financial Management and Accounting Systems Problems Are Targeted by the CFO Act

The federal government manages hundreds of programs, many of them individually larger than our nation's biggest publicly owned corporations, without adequate knowledge of their financial condition and results achieved. Widespread financial management weaknesses cripple our leaders' efforts to effectively manage and oversee federal programs. For example, recent audits have found the following:

-- The financial records of the Army and the Air Force required over $200 billion in adjustments to improve the accuracy of related financial reports.

-- The National Aeronautics and Space Administration's year-end financial reports to the Treasury Department contained over $500 million in errors.

-- The government's accounting control over the almost $2 billion Indian Trust Fund has been so poor that it has been unable to reconcile accounts for over half a century, and the Fund has incurred millions of dollars in unnecessary losses.

-- The Department of Veterans Affairs lacks information on the operating costs of its 172 hospitals and, as a result, program managers cannot determine which facilities are working well and which procedures are not cost-effective.

The government can no longer afford to operate this way. It must address three major areas of weakness: inadequate or erroneous financial data, unreliable financial systems and controls, and the general lack of results-oriented reports on financial condition and operating performance.

Our financial audits of the larger federal agencies regularly identify tens of billions of dollars in accounting errors as well as serious gaps in information. These problems undermine the government's ability to effectively perform basic financial management functions, make informed decisions, and conduct adequate oversight of taxpayer funds. Further, breakdowns in financial systems and controls not only waste billions of dollars, but also reinforce the deeply rooted public perception that the government cannot effectively manage the taxpayers' money. Finally, while the government has a flood of cash-based information, it has collected little data to monitor the cost of programs and to measure their performance. This makes it extremely difficult to manage effectively, determine results achieved with public funds, and establish reasonable spending priorities.

## The CFO Act provides the roadmap to reform

A growing consensus on the seriousness of the government's financial management problems culminated in the November 1990 enactment of the Chief Financial Officers (CFO) Act. Senator Glenn, you and the members of this Committee are to be commended for being a driving force behind passage of this legislation--the most far-reaching financial management legislation in 40 years and one that provides an excellent blueprint for reform.

To address the historic lack of priority given to financial management, the act established a much needed leadership structure consisting of a new Deputy Director for Management and a Controller in OMB and professionally qualified CFOs in all major departments. These CFOs are to report directly to agency heads and are to be given broad authority for financial management. Also, the act establishes a CFO Council to address common issues.

The CFO framework offers great hope for improving government management, but the government is a long way from achieving the act's objectives and fixing its high-risk problems. While some progress has been made, a greater sense of urgency is needed in solving the problems. The tone of top management will be very important in sustaining and building upon current improvement initiatives. Changing a government culture, which has not always seen financial management as important, is difficult, especially if efforts are not sustained or are not perceived as important.

Without concerted action to implement the CFO Act, including attention by the new President and the Cabinet and strong support by agency program managers, the government will remain devoid of accountability, hampered in its ability to make informed decisions, and embarrassingly unable to explain the results achieved by the use of trillions of dollars collected from the nation's citizens. The Congress made its expectations clear when it enacted the landmark CFO legislation as a bipartisan initiative. Its continued support and additional oversight and actions by the President and OMB are critical.

Along this line, as you know from our testimony on the Army financial audit, the broad scope pilot efforts required by the CFO Act have produced significant benefits, as acknowledged by Army Secretary Stone. The act's pilot project will need to be renewed this summer if the program is to continue. We hope that you will continue your support of the agencywide audits and of the act's other provisions.

Further, we believe that the Congress should

-- amend the CFO Act to require audited financial statements on an annual basis for all major agencies and the government overall,

-- focus closely on CFO appointments to ensure the qualifications of these individuals,

-- conduct annual oversight hearings using the CFOs' annual reports and audited financial statements, and

-- provide necessary funding support for financial reform efforts through investments in modern systems, personnel development, expanded financial reporting and auditing, and a strengthened Office of Federal Financial Management.

## Information Management and Technology Deficiencies Are Widespread and Costly

The federal government spends over $20 billion annually on new technology--and tens of billions more running current systems. Despite the magnitude of this investment, agency after agency still lacks critical information needed to analyze programmatic issues, manage agency resources, control expenditures, and demonstrate measurable results.

The effect of information systems management weaknesses is demonstrated by the following examples:

-- Poor information systems are aggravating the current crisis in health care financing. Medicare, for example, mistakenly paid out over a billion dollars for services already covered by other insurers, in part because of inadequate data. Equally important, patient care and the related reimbursement and insurance systems still heavily depend on paper records that intrinsically limit the capacity to retrieve and process critical data. A recent estimate indicated that better use of electronic interchange could yield cost savings of $4 billion to $10 billion annually.

-- During the past 25 years, the Internal Revenue Service has twice tried and failed to modernize its antiquated tax-processing system. Unreliable and unresponsive, this system impedes IRS's ability to collect and account for tax revenues, deal with a reported (but much overstated) $111 billion in accounts receivable, and narrow the annual tax gap estimated at about $114 billion for 1992.

Sound information systems management is essential for realizing potential productivity and effectiveness gains achievable with today's technology. Agency leaders need to make their information management organization a strong partner in determining how to efficiently meet the strategic needs of the agency. Agency leaders must adopt a management philosophy that emphasizes continuous improvement of business practices. However, top federal executives continue to overlook the strategic role of information technology in reengineering business practices. Moreover, information resource managers typically lack the authority and resources needed to help their agencies modernize and simplify work practices, define information needs, and ensure the most effective use of information resources.

The federal acquisition management and budget processes aggravate this situation. The demand for certainty in the system development process leads project managers to downplay risks and problems--resulting in missed benefits and misspent money. Solving these problems will depend heavily on the ability of top executives to both develop a strategic framework for change and effectively marshal their agencies' information resources talent. In addition, both agencies and the Congress need to be willing to experiment with different approaches to acquisition management and budget processes. Experimentation may lead to broad-based agreement on better acquisition management models that could help agencies build the information technology base they need to dramatically improve their operations and better serve the American people.

The Congress, the President, and the Office of Management and Budget must play active roles in correcting the government's information management problems. In this area, the Congress should, among other things,

-- ensure that OMB has appropriate leadership, staff resources, and funding to strengthen its management function in information technology;

-- focus closely on the confirmation of the appointment of the Director of the Office of Information and Regulatory Affairs to ensure the qualifications of this individual;

-- hold agency heads accountable for developing and following a strategic framework for reengineering business processes that involves the information systems function in decision-making; and

-- support and monitor agency experiments in using innovative methods for budgeting and managing large-scale information technology acquisitions.

## Breakdowns in General Management Functions Exist Throughout Federal Programs and Operations

Over the years, our work has identified extensive management problems across the spectrum of federal activities: important program objectives are not being met, funds are wasted, major projects are over budget and behind schedule, and monies due are not collected. These problems have existed for many years and efforts to correct them have resulted in incremental improvements to the overall system of management, such as better cash and debt management. But in too many cases, management problems persist long after they have been brought to light and long after agencies have agreed to correct them. This occurs because the piecemeal actions taken have not effectively addressed the root causes of these problems.

Identifying the problems is not enough. Policymakers and managers need to understand the sources of the problems in the first place and then systematically change them by attacking their root causes. At least three fundamental conditions individually and collectively present formidable obstacles to good management.

-- Diffused accountability for program results. The Congress, the President, and individual federal agencies have yet to create a results-oriented environment in which managers focus on a program's results--such as reducing childhood diseases--and not just on producing an output--such as administering vaccines. Often the results agencies are trying to achieve or who is responsible for doing what is not clear.

-- Short-term mentality deters good management. Several factors create an environment that encourages short-term actions in the face of long-term management problems. First, top positions often are filled by political appointees who generally do not focus on long-term management issues. Second, the budget process focuses on single-year increments and is cash based; therefore, it does not provide sufficient perspective on the long-term costs and benefits of policy choices. And third, sustained cuts in agency operating budgets and underinvestment in public service have diminished the ability to manage well.

-- Government machinery inhibits results-oriented action. Traditionally, central management agencies have tried to control and regulate line agency actions. Programs and statutes with similar objectives are scattered across and applicable to various agencies or subcomponents. Further, complex organizational networks and overlapping statutes have evolved in various program areas over the years. These complicate the government's ability to establish accountability, set priorities, and focus its resources on accomplishing stated objectives.

It is time to address these problems, and the Congress, the President, and the Office of Management and Budget each has a role. The Congress should

-- promptly consider legislation to require agencies to articulate their goals and missions, develop implementation plans and measures tied to their missions, and report annually on program results;

-- ensure that OMB has the appropriate resources to ensure effective leadership in the management arena;

-- continue support for the effective implementation of the CFO Act and the Pay Reform Act; and

-- support agency innovation through the use of pilots and grants of flexibility in selected policy areas.

## CONCLUSIONS

Over the past 3 years, initiatives by the Congress, the administration, and federal agency officials suggest a renewed interest in and willingness to face up to widespread and costly problems in federal programs. However, it is too early to evaluate the impact of these actions on the condition of these programs; their vulnerability to fraud, waste, abuse, and mismanagement; and their ability to reduce or eliminate losses and make the programs more efficient and effective.

Clearly, however, the government cannot afford to falter in its efforts to bring these initiatives to completion and to build upon its successes while learning from its mistakes. We must develop new and innovative ways to strengthen federal programs and rekindle the American taxpayer's faith in our ability to manage federal programs.

While the Congress can help, the administration--the President and OMB--will be the force that can ensure real progress here. If the new administration will do its part and intensify efforts to deal with the specific high-risk areas we and OMB have targeted and adopt the overall recommendations we have made in the transition reports, we should see a rapid reduction in both the number and severity of high-risk problems and in the incidence of fraud, waste, abuse, and mismanagement.

The continuation of several specific activities is also essential. All provisions of the Chief Financial Officers Act must be implemented. Unfortunately, the results of our high-risk and other audits show that we have a long way to go before we can claim success in this area. Financial management and information resource management problems are pervasive; agency internal control systems often provide little, if any, assurance that programs are operating as intended; and few agencies have developed meaningful performance measures for use in evaluating program operations.

Despite this reality, we must not give up hope. The Congress, the administration, and agency management must remain committed to the objectives of the act and work to satisfy those purposes. The transition series reports on financial management, information management, and general management contain recommendations to the Congress, the President, and the Office of Management and Budget that, if acted upon, should help strengthen the management and operation of federal programs and reduce losses due to fraud, waste, abuse, and mismanagement.

Finally, we must recognize that our high-risk program is currently examining only 17 areas. Even adding OMB's high-risk program (which includes about 100 areas) to ours, these programs cover only a small percentage, at best, of the problem areas throughout the government. The Congress, the administration, and agency officials must remain diligent in overseeing efforts to correct all problems identified in federal programs, not just those identified through high-risk programs or the annual reports required by the Financial Integrity Act. The corrective actions needed may be relatively easy to implement or they may require new or significantly amended legislation or governmentwide directives. Regardless of the complexity and difficulty of implementing needed corrective actions, they must be pursued to completion.

For our part, we will continue to review the spectrum of federal programs and activities to ensure that we remain focused on the most important high-risk areas.

Mr. Chairman, that concludes my prepared statement. At this time, I will be glad to respond to any questions you or other Committee members have.

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