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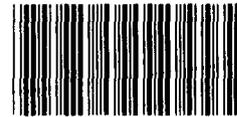
Testimony

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Improving Internal Controls  
and Accounting

Statement of  
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Before the  
Legislative Commission on Public Management  
Systems  
State of New York



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Mr. Chairman and Members of the Commission:

We are very pleased to appear today to discuss the importance of internal controls and the experience of the federal government since passage of the Federal Managers' Financial Integrity Act of 1982.

#### BACKGROUND

The Financial Integrity Act provided for the first time the needed discipline on a governmentwide basis to identify and remedy long-standing internal control and accounting system problems that hamper effectiveness and accountability, cost the taxpayer potentially billions of dollars, and erode the public's confidence in government.

The act, which was strongly supported by the Comptroller General of the United States, places primary responsibility for adequate systems of internal control and accounting with management--not with the auditor or accountant but with management.

To provide the framework for implementation, as prescribed by the act, the Comptroller General issued internal control standards. These standards apply to program management, as well as financial management areas, and encompass all operations and administrative functions. In short, the federal government views internal controls as being synonymous with management controls.

The Financial Integrity Act is a rather straightforward, two-page law. It requires federal agencies, in accordance with guidelines established by the Office of Management and Budget, to annually assess their internal control and accounting systems and report their status to the President and the Congress. This process focuses attention on the need for effective controls and accounting and on the risks associated with poor systems.

The annual reporting requirement has been important to the success of the act. In the annual report, the agency head must identify material system weaknesses and briefly describe planned corrective actions. The annual report serves two purposes:

- It requires agency heads to make a formal statement on the status of their systems (that is, to put their name on the dotted line).
- It provides a mechanism for tracking the progress of agencies in improving their systems, which is the bottom line of the act.

#### IMPACT OF THE ACT

Although the federal government is far from having the quality systems we would like to see, the Financial Integrity Act has had an important impact over the past 4 years.

- First, agencies have identified over a thousand material weaknesses, with additional weaknesses being identified each year.
- Second, agencies have extensive efforts under way to strengthen their systems and have reported correcting hundreds of material weaknesses.
- Finally, managers' awareness of the importance of good internal control and accounting systems has increased, and additional attention has been placed on correcting long-standing problems.

## LESSONS LEARNED

Based on 4 years of experience with the Financial Integrity Act, I would like to highlight several lessons learned:

- First, top management commitment and support is very important. Managers must be clearly shown that the process required by the act will help them to better carry out their responsibilities. Although the auditor plays an important role, the job of running an organization, with sound controls and accounting, will not be a reality without strong management commitment.
- Second, managers must understand the act and its application. The federal government developed extensive internal control training programs. By its nature, internal control terminology can be most difficult to those not familiar with accounting. If, however, you can show managers that what we are talking about is management controls--the whole network of policies, procedures, practices, and systems--then they begin to embrace this concept.
- Third, evaluation programs must be reliable and useful. They cannot take on a life of their own or be seen as a paper exercise. This became a serious problem in the federal government, which has worked to reduce the paperwork and to make the evaluation requirements more understandable to the nonaccountant.
- Fourth, in evaluating the adequacy of internal controls and accounting systems, there is a need to test the systems in operation and to evaluate ADP controls, which are integral to most systems today.

- Fifth, by virtue of their training and experience, auditors must play an important role in making the act work. In the federal government, the General Accounting Office and the inspectors general not only evaluated and reported on internal controls and accounting systems as part of their normal audits but also provided oversight and technical assistance, helped devise and conduct training programs, and consulted on internal controls and accounting.
  
- Finally, expect the first year or two to be a learning experience. In the federal government, we have seen steady progress and, as I outlined earlier, some important results. But it has taken a lot of hard work and time, and a lot remains to be done to strengthen internal controls and accounting.

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Mr. Chairman, this concludes my remarks. We appreciate the opportunity to appear before the Commission and would be pleased to respond to any questions you or members of the Commission may have at this time.