



United States  
General Accounting Office  
Washington, D.C. 20548

161206

Accounting and Information  
Management Division

B-281057

September 25, 1998

The Honorable John R. Kasich  
Chairman, Committee on the Budget  
House of Representatives

Subject: Financial Audit Results: Impact on Budgetary Information

Dear Mr. Chairman:

Beginning in December 1996, with our first report to you on Forest Service financial management issues, we have been providing your office with analyses of the potential budgetary and programmatic implications of the results of the financial audits of the Forest Service,<sup>1</sup> Federal Aviation Administration,<sup>2</sup> and the Navy.<sup>3</sup> In these reports, we pointed out major inadequacies in the way in which the agencies manage and control funds provided to carry out their missions. We also recently responded to your request<sup>4</sup> for examples of the cost of waste, fraud, abuse and mismanagement in major federal programs. These examples were drawn from audits of agency financial statements and from reports issued by GAO and the Inspectors General.

As requested by your office, this letter describes what can be learned from the results of the audit of the fiscal year 1997 consolidated financial statements of

---

<sup>1</sup>Letter dated December 20, 1996, to the Chairman, House Committee on the Budget (GAO/AIMD-97-11R); Financial Management: Forest Service's Progress Toward Financial Accountability (GAO/AIMD-97-151R, August 29, 1997); Forest Service: Status of Progress Toward Financial Accountability (GAO/AIMD-98-84, February 27, 1998).

<sup>2</sup>Financial Management: Federal Aviation Administration Lacked Accountability for Major Assets (GAO/AIMD-98-62, February 18, 1998).

<sup>3</sup>CFO Act Financial Audits: Programmatic and Budgetary Implications of Navy Financial Data Deficiencies (GAO/AIMD-98-56, March 16, 1998).

<sup>4</sup>Letter to the Chairman, House Committee on the Budget, dated September 14, 1998, on the cost of mismanagement (GAO/AIMD-98-265R).

161206

the federal government about the reliability of financial data included in agency budget information presented to Congress.

Beginning in fiscal year 1996, under requirements of the Government Management Reform Act, financial statements are being routinely prepared and independently audited for the government's largest 24 departments and agencies. Also, for fiscal year 1997, the first set of consolidated financial statements was prepared for the U.S. government and audited by GAO. Progress is being made in improving financial management, with 10 of 24 departments and agencies receiving an unqualified opinion on their financial statements for fiscal year 1997. However, 14 agencies have not yet been able to obtain an unqualified audit opinion on their financial statements. Also, as you know, we were unable to form an opinion on the reliability of the consolidated financial statements because of major deficiencies which were identified during the audit process.<sup>5</sup>

In our March 31, 1998, report on the consolidated financial statements, we noted that significant financial systems weaknesses, problems with fundamental recordkeeping, incomplete documentation, and weak internal controls, including computer controls, prevented the government from accurately reporting a large portion of its assets, liabilities, and costs. These deficiencies affected the reliability of the consolidated financial statements and much of the underlying financial information. They also affected the government's ability to accurately measure the full cost and financial performance of programs, effectively and efficiently manage its operations, and ensure compliance with laws and regulations. Further, many of the issues disclosed in the audit report can also affect the ability of agencies to report accurately on budget execution and to project for future budgetary needs.

For example, as we pointed out in our report, various agencies were unable to reliably:

- Determine the level of property, equipment, materials, and supplies on hand or the cost of these assets. This lack of accountability for this major category of assets affects certain agencies' (including the Department of Defense, the Federal Aviation Administration, and the Forest Service) ability to accurately predict future budgetary needs for asset acquisitions, maintenance, and related costs.

---

<sup>5</sup>Financial Audit: 1997 Consolidated Financial Statements of the United States Government (GAO/AIMD-98-127); U.S. Government Financial Statements: Results of GAO's Fiscal Year 1997 Audit (GAO/T-AIMD-98-128).

- Estimate the cost of federal credit programs and, in some cases, determine the face value of loans and loan guarantees outstanding. Until affected agencies (including the Departments of Agriculture, Veterans Affairs, and Housing and Urban Development) complete corrective action, information supplied by them in their annual budget requests for credit programs will not be based on reliable data.
- Assess the estimated cost of disposing of hazardous waste and cleaning up environmental contamination. The major problem in this area is related to the fact that DOD had not fully estimated the cost of disposing of major weapons systems. Properly stating these liabilities could assist in determining priorities for cleanup activities and allow for appropriate consideration of future budgetary resources needed to carry out these activities.
- Reconcile their records of cash disbursements with those of the Department of the Treasury, leaving billions of dollars of unresolved differences outstanding as of the end of fiscal year 1997. In addition, large amounts of other unresolved differences were arbitrarily written off by some agencies without determining whether their records could, in fact, have been correct. This is similar in concept to individuals or private companies being unable to balance their checkbooks and simply adjusting them to their banks' records. Because most assets, liabilities, revenues, and expenses stem from or result in cash transactions, errors in the receipt or disbursement data affect the accuracy of various U.S. government reports, including budget execution reports.

These examples and other findings reported as a result of the consolidated and agency financial statement audits suggest that some data presented in agency budget requests concerning prior year obligations and expenditures may not be fully reliable. However, it is difficult to quantify the extent of this problem because (1) historically, the systems used for budgetary reporting are different from those used for financial reporting and (2) to date, budgetary reporting systems have not been separately audited nor reconciled fully to audited financial statements.

This problem is being addressed as part of the financial management reforms mandated by the Chief Financial Officers Act, the Government Management Reform Act, and the Federal Financial Management Improvement Act. The first part of this reform effort has focused on the development of basic financial management and reporting systems. While serious issues surrounding the reliability of reported information still remain, most agencies are now able to prepare basic financial statements. Beginning with fiscal year 1998, agencies are scheduled to provide more explicit information in the financial statements

on the status of budgetary resources and outlays and to reconcile this information with the net cost of operations reported in the Statement of Net Cost.

There is a critical need for this link between financial statements and budgetary reporting. As the Overview of Federal Accounting Concepts and Standards states, "Federal financial reporting should assist in fulfilling the government's duty to be publicly accountable for monies raised through taxes and other means . . . . Federal financial reporting should provide information that helps the reader to determine

- how budgetary resources have been obtained and used and whether their acquisition and use were in accordance with legal authorization,
- the status of budgetary resources, and
- how information on the use of budgetary resources relates to information on the costs of program operations and whether information on the status of budgetary resources is consistent with other accounting information on assets and liabilities."

As part of the fiscal year 1998 financial statement audits, agency auditors and GAO will be assessing the reported budgetary information and reconciliations of financial and budgetary information. It is expected that some agencies will initially have difficulty preparing the reconciliations; therefore, the near-term usefulness of this information could be somewhat limited for those agencies. We will be working with OMB, chief financial officers, and Inspectors General to address problems encountered in the preparation and audit of this information. Also, in the coming year, we plan to test selected specific information concerning prior year obligations and expenditures included in agency budget information presented to Congress.

As agencies progress in their ability to prepare budgetary reports and reconciliations of budgetary and financial statement information, and as that financial statement information becomes more reliable, confidence in the accuracy and reliability of the budgetary information used to manage and make critical decisions about the use of taxpayer funds to carry out federal agencies' missions will be enhanced.

-----

B-281057

Please feel free to call me at (202) 512-8341 or Paul Posner, Director, Budget Issues, at (202) 512-9573, to further discuss these issues.

Sincerely yours,

A handwritten signature in cursive script that reads "Linda Calbom".

Linda M. Calbom  
Director, Resources, Community, and  
Economic Development Accounting  
and Financial Management Issues

(919316)



---

  

---

### Ordering Information

**The first copy of each GAO report and testimony is free. Additional copies are \$2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. VISA and MasterCard credit cards are accepted, also. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.**

**Orders by mail:**

**U.S. General Accounting Office  
P.O. Box 37050  
Washington, DC 20013**

**or visit:**

**Room 1100  
700 4th St. NW (corner of 4th and G Sts. NW)  
U.S. General Accounting Office  
Washington, DC**

**Orders may also be placed by calling (202) 512-6000  
or by using fax number (202) 512-6061, or TDD (202) 512-2537.**

**Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (202) 512-6000 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.**

**For information on how to access GAO reports on the INTERNET, send an e-mail message with "info" in the body to:**

**[info@www.gao.gov](mailto:info@www.gao.gov)**

**or visit GAO's World Wide Web Home Page at:**

**<http://www.gao.gov>**

---

**United States  
General Accounting Office  
Washington, D.C. 20548-0001**

**Bulk Rate  
Postage & Fees Paid  
GAO  
Permit No. G100**

**Official Business  
Penalty for Private Use \$300**

**Address Correction Requested**

---