

TRANSFORMATION *Challenges*



**The Honorable
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Comptroller General
of the United States

Maryland Association
of CPAs (MACPA)
Conference
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GAO's Strategic Plan

SERVING THE CONGRESS AND THE NATION GAO'S STRATEGIC PLAN FRAMEWORK

MISSION

GAO exists to support the Congress in meeting its constitutional responsibilities and to help improve the performance and ensure the accountability of the federal government for the benefit of the American people.

THEMES

Long-Term
Fiscal Imbalance

National
Security

Global
Interdependence

Changing
Economy

Demographics

Science
and Technology

Quality
of Life

Governance

GOALS & OBJECTIVES

Provide Timely, Quality Service to the Congress and the Federal Government to ...

Address Current and Emerging Challenges to the Well-Being and Financial Security of the American People *related to ...*

- Health care needs and financing
- Education and protection of children
- Work opportunities and worker protection
- Retirement income security
- Effective system of justice
- Viable communities
- Natural resources use and environmental protection
- Physical infrastructure

Respond to Changing Security Threats and the Challenges of Global Interdependence *involving ...*

- Emerging threats
- Military capabilities and readiness
- Advancement of U.S. interests
- Global market forces

Help Transform the Federal Government's Role and How It Does Business to Meet 21st Century Challenges *by assessing ...*

- Roles in achieving federal objectives
- Government transformation
- Key management challenges and program risks
- Fiscal position and financing of the government

Maximize the Value of GAO by Being a Model Federal Agency and a World-Class Professional Services Organization *in the areas of ...*

- Client and customer satisfaction
- Strategic leadership
- Institutional knowledge and experience
- Process improvement
- Employer of choice

CORE VALUES

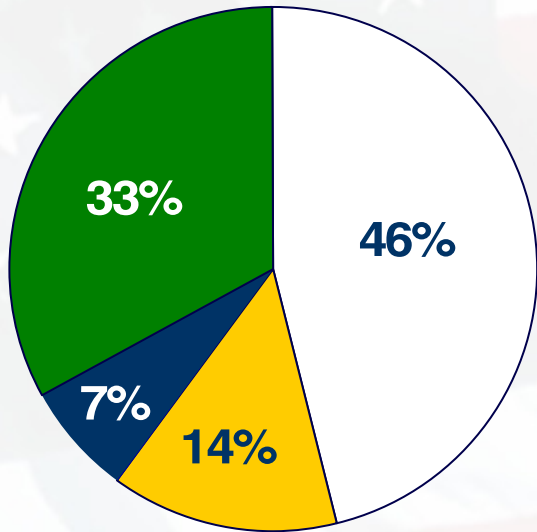
Accountability

Integrity

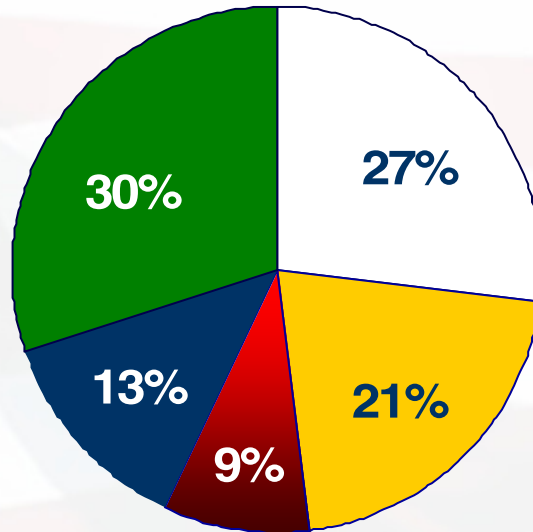
Reliability

Composition of Federal Spending

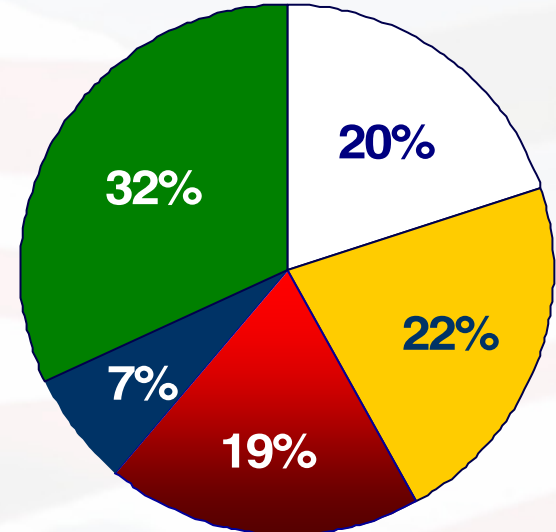
1964



1984



2004



Defense
Net interest

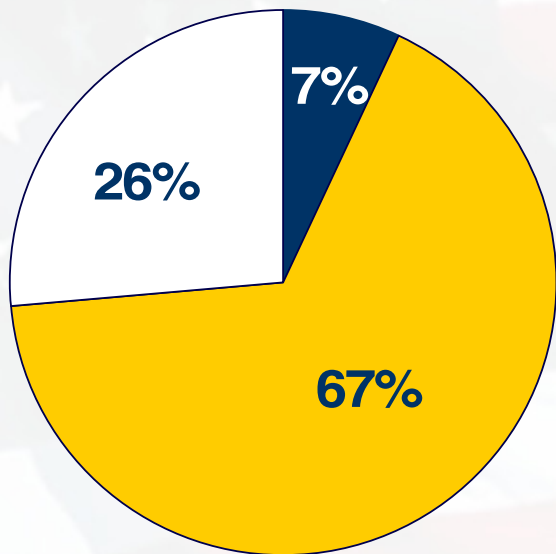
Social Security
All other spending

Medicare & Medicaid

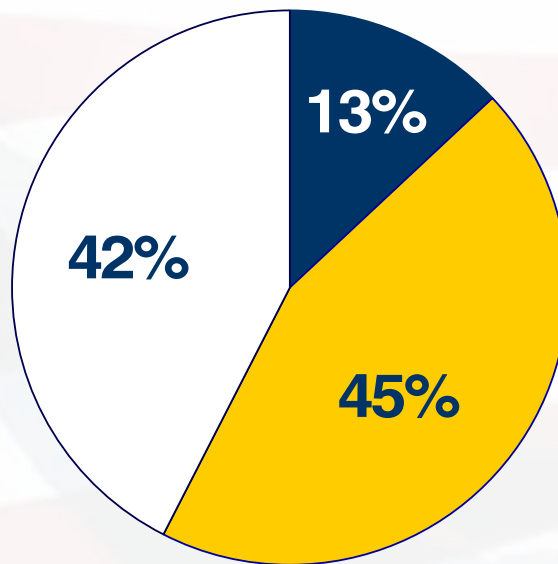
Source: Office of Management and Budget.

Federal Spending for Mandatory and Discretionary Programs

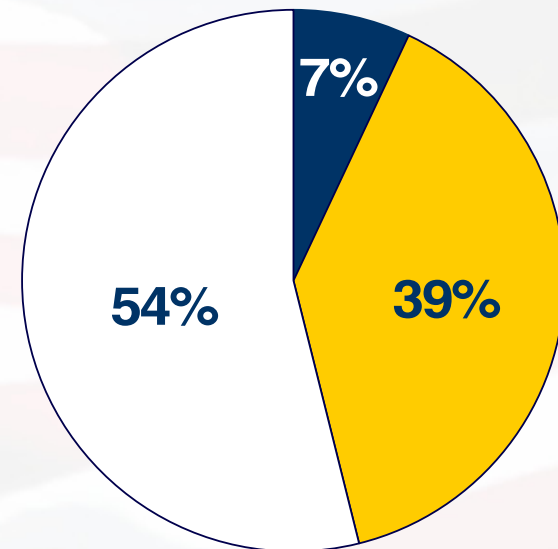
1964



1984



2004



 **Net Interest**

 **Discretionary**

 **Mandatory**

Source: Office of Management and Budget.

Fiscal Year 2004 Deficit Numbers

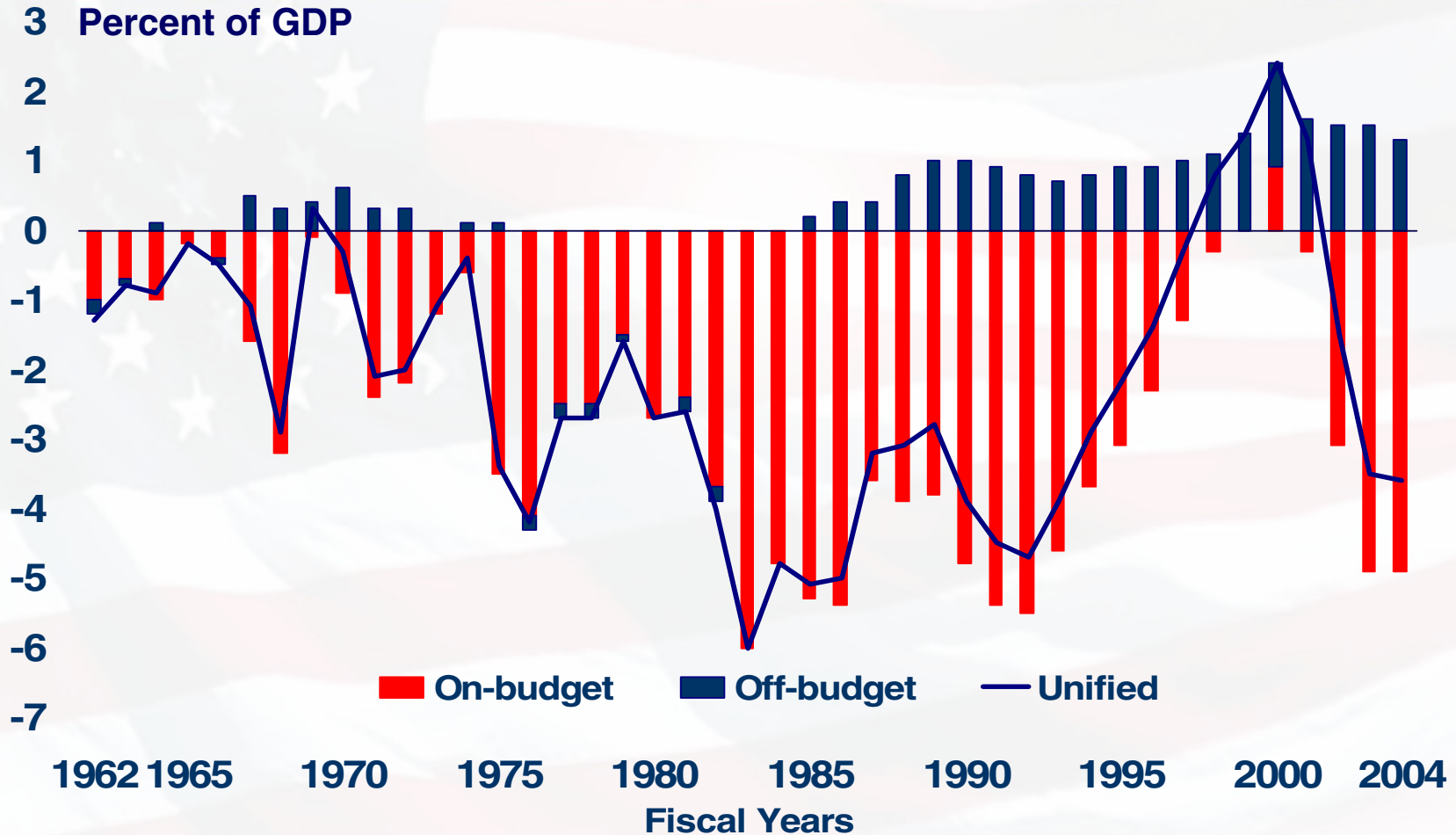
	\$ Billion	% of GDP
On-Budget Deficit	(567)	(4.9)
Off-Budget Surplus	155*	1.3
Unified Deficit	(412)	(3.6)

*Includes the \$151 billion Social Security surplus and a \$4 billion surplus for the Postal Service

March 2005

Surplus or Deficit as a Share of GDP

Fiscal Years 1962-2004



Source: Office of Management and Budget and Congressional Budget Office.

Selected Fiscal Exposures: Sources and Examples 2005^a

Type	Example (dollars in billions)
Explicit liabilities	Publicly held debt (\$4,297) Military and civilian pension and post-retirement health (\$3,059) Veterans benefits payable (\$925) Environmental and disposal liabilities (\$249) Loan guarantees (\$43)
Explicit financial commitments	Undelivered orders (\$596) Long-term leases (\$39)
Financial contingencies	Unadjudicated claims (\$4) Pension Benefit Guaranty Corporation (\$96) Other national insurance programs (\$1) Government corporations e.g., Ginnie Mae
Exposures implied by current policies or the public's expectations about the role of government	Debt held by government accounts (\$3,071) ^b Future Social Security benefit payments (\$4,017) ^c Future Medicare Part A benefit payments (\$8,561) ^c Future Medicare Part B benefit payments (\$12,384) ^c Future Medicare Part D benefit payments (\$8,686) ^c Life cycle cost including deferred and future maintenance and operating costs (amount unknown) Government Sponsored Enterprises e.g., Fannie Mae and Freddie Mac

^a All figures are for end of fiscal year 2004, except Social Security and Medicare estimates, which are as of January 1, 2005.

^b This amount includes \$845 billion held by military and civilian pension and post-retirement health funds that would offset the explicit liabilities reported by those funds.

^c Figures for Social Security and Medicare are net of debt held by the trust funds (\$1,687 billion for Social Security, \$268 billion for Medicare Part A, and \$19 billion for Medicare Part B) and represent net present value estimates over a 75-year period. Over an infinite horizon, the estimate for Social Security would be \$11.1 trillion, \$24.1 trillion for Medicare Part A, \$25.8 trillion for Medicare Part B, and \$18.2 trillion for Medicare Part D.

Source: GAO analysis of data from the Department of the Treasury, the Office of the Chief Actuary, Social Security Administration, and the Office of the Actuary, Centers for Medicare and Medicaid Services.

Revised 3/29/05

Current Fiscal Policy Is Unsustainable

- **The “Status Quo” is Not an Option**
 - We face large and growing structural deficits largely due to known demographic trends and rising health care costs.
 - GAO’s simulations show that balancing the budget in 2040 could require actions as large as
 - Cutting total federal spending by about 60 percent or
 - Raising taxes to about 2.5 times today's level
- **Faster Economic Growth Can Help, but It Cannot Solve the Problem**
 - Closing the current long-term fiscal gap based on responsible assumptions would require real average annual economic growth in the double digit range every year for the next 75 years.
 - During the 1990s, the economy grew at an average 3.2 percent per year.
 - As a result, we cannot simply grow our way out of this problem. Tough choices will be required.
- **The Sooner We Get Started, the Better**
 - Less change would be needed, and there would be more time to make adjustments.
 - The miracle of compounding would work with us rather than against us.
 - Our demographic changes will serve to make reform more difficult over time.

The Way Forward

- Implement new accounting and reporting approaches and new budget control mechanisms for considering the impact of spending and tax policies and decisions over the long term
- Develop new metrics for measuring the impact of policies and decisions over the long term (e.g., key national indicators to measure our Nation's position and progress over time and in relation to other countries)
- Reexamine the base—question existing programs, policies and activities

We Need a Multifaceted Approach to Close the Long-Term Fiscal Gap

Policy:

- Restructure existing entitlement programs
- Reexamine the base of discretionary and other spending
- Review and revise our tax policy and enforcement programs

Operations:

- Reassess and revise how the government does business (e.g., management, planning and operational issues)
- Consider who should provide government services (e.g., sourcing strategy)
- Consider how the government should finance its operations

GAO's High-Risk List

2005

High-Risk Areas	Designated High Risk
Addressing Challenges in Broad-based Transformations	
Protecting the Federal Government's Information Systems and the Nation's Critical Infrastructures	1997
Strategic Human Capital Management ^a	2001
U.S. Postal Service Transformation Efforts and Long-Term Outlook ^a	2001
Managing Federal Real Property ^a	2003
Implementing and Transforming the Department of Homeland Security	2003
Establishing Appropriate and Effective Information-Sharing Mechanisms to Improve Homeland Security	2005
DOD Approach to Business Transformation ^a	2005
DOD Supply Chain Management (formerly Inventory Management)	1990
DOD Weapon Systems Acquisition	1990
DOD Business Systems Modernization	1995
DOD Financial Management	1995
DOD Support Infrastructure Management	1997
DOD Personnel Security Clearance Program	2005
Managing Federal Contracting More Effectively	
DOE Contract Management	1990
NASA Contract Management	1990
DOD Contract Management	1992
Management of Interagency Contracting	2005
Assessing the Efficiency and Effectiveness of Tax Law Administration	
Enforcement of Tax Laws ^{a, b}	1990
IRS Business Systems Modernization ^c	1995
Modernizing and Safeguarding Insurance and Benefit Programs	
Medicare Program ^a	1990
HUD Single-Family Mortgage Insurance and Rental Housing Assistance Programs	1994
Medicaid Program ^a	2003
Modernizing Federal Disability Programs ^a	2003
Pension Benefit Guaranty Corporation Single-Employer Insurance Program ^a	2003
Other	
FAA Air Traffic Control Modernization	1995

^a Legislation is likely to be necessary, as a supplement to actions by the executive branch, in order to effectively address this high-risk area.

^b Two high-risk areas—Collection of Unpaid Taxes and Earned Income Credit Noncompliance—have been consolidated to make this area.

^c The IRS Financial Management high-risk area has been incorporated into this high-risk area.

21st Century Challenges Report

- Report was issued February 16
- Based on GAO's work for the Congress
- Provides framework and questions to assist in reexamining the base
- Covers entitlements & other mandatory spending, discretionary spending, and tax policy and programs

Generic Reexamination Criteria and Sample Questions

Relevance of purpose and the federal role

Why did the federal government initiate this program and what was the government trying to accomplish?

Have there been significant changes in the country or the world that relate to the reason for initiating it?

Measuring success

Are there outcome-based measures? If not, why?

If there are outcome-based measures, how successful is it based on these measures?

Targeting benefits

Is it well targeted to those with the greatest needs and the least capacity to meet those needs?

Affordability and cost effectiveness

Is it using the most cost-effective or net beneficial approaches when compared to other tools and program designs?

Best practices

Is the responsible entity employing prevailing best practices to discharge its responsibilities and achieve its mission?

Twelve Reexamination Areas

MISSION AREAS

- Defense
- Education & Employment
- Financial Regulation & Housing
- Health Care
- Homeland Security
- International Affairs
- Natural Resources, Energy & Environment
- Retirement & Disability
- Science & Technology
- Transportation

CROSSCUTTING AREAS

- Improving Governance
- Reexamining the Tax System

Themes

- Changing Security Threats
- Increasing Global Interdependence
- Demographic Shifts—Aging Population
- Promoting Growth in a Knowledge-Based Economy
- Governance Challenges

Illustrative 21st Century Questions

- How should the historical allocation of resources across services and programs be changed to reflect the results of a forward-looking comprehensive threat/risk assessment as part of DOD's capabilities-based approach to determining defense needs?
- Should federally funded training programs operated across multiple federal agencies—9 federal agencies administer 44 such programs—be better integrated and restructured in order to increase their cost effectiveness?
- To what extent do the tools and incentives increase spending on housing rather than promote affordable housing? Can the tools and incentives provided to homeownership be better targeted toward increasing home ownership among selected groups with less capacity to access credit markets?

Illustrative 21st Century Questions

- How can industry standards for acceptable care be established and payment reforms be designed to bring about reductions in unwarranted medical practice variation? For example, what can or should the federal government do to promote uniform standards of practice for selected procedures and illnesses?
- What criteria should be used to target federal funding for homeland security in order to maximize results and mitigate risk within available resource levels?
- Do we need to reexamine the U.S. force structure used for nation building and peacekeeping activities by the United Nations, NATO, and other international institutions? Should the United States have a separate force devoted to such functions? What role should the United Nations, NATO, and other international institutions perform in connection with such functions?

Illustrative 21st Century Questions

- To what extent are federal energy policies and incentive structures adequately preparing the nation to satisfy its energy needs over the long term? What is the appropriate balance between efforts to promote enhanced production of fossil fuels, alternative renewable energy sources, and energy conservation?
- How can federal disability programs, and their eligibility criteria, be brought into line with the current state of science, medicine, technology, and labor market conditions?
- How can the United States better develop a world-class technical and scientific domestic workforce that is not as dependent on large inflows of international students and researchers?

Illustrative 21st Century Questions

- Can intermodal solutions to the needs of modes such as freight, air, and passenger rail service be effectively carried out within the framework of the existing trust funds and other transportation programs or is another model needed?
- Is the federal government effectively informed by a key national indicator system about the position and progress of the nation as a whole—both on an absolute and relative bases compared to other nations—as a guide to helping set agency and program goals and priorities?
- Which tax incentives need to be reconsidered because they fail to achieve the objectives intended by the Congress, their costs outweigh their benefits, they duplicate other programs, or other more cost-effective means exist for achieving their objectives

Where Do We Go from Here?

- Reexamining the base of government will take many years
- Various reexamination approaches already exist and have been used by the federal government
- Some states and other nations offer models of reexamination
- Early action on reexamination has significant benefits

GAO's Work to Modernize the Accountability Profession

GAO is actively working to modernize and transform the accountability profession, both inside the government and in the private sector, and to lead by example in this area.

- Definition of success in financial management: clean opinion, no major weaknesses in controls or compliance, and financial systems that produce timely, accurate and useful information for management
- Opinion on system of internal control
- 2003 revision of *Government Auditing Standards*
- Creation of the U.S Auditing Standards Coordinating Forum (i.e., GAO, PCAOB, ASB)
- Coordination with accountability organizations around the world (e.g., INTOSAI)
- Modernization of the accounting/reporting and audit models
- Assure appropriate treatment of restatements by auditors and others
- Monitor implementation of the Sarbanes-Oxley Act, including providing suggestions for possible actions by the PCAOB and the SEC in connection with the internal control reporting requirements under Section 404
- Consider whether reform elements similar to those in Sarbanes-Oxley make sense for the federal government

Sarbanes-Oxley Act Implementation:

What We Have Learned and Future Directions

- The Sarbanes-Oxley Act reforms are sound and necessary
- Reforms have improved governance and management, including the involvement of the board, audit committees, and top management in financial reporting and internal control issues.
- Implementing section 404 has been challenging due to:
 - The amount and nature of internal control work performed in the past
 - Extensive audit work being performed due to real and/or perceived lack of flexibility in PCAOB Auditing Standard No. 2
 - Significant first-year implementation efforts

What We Have Learned and Future Directions (cont'd)

- We strongly support the concepts behind section 404. However, we believe that economies and efficiencies can be gained in the process through:
 - Auditor and management efficiencies and streamlining in the second year and beyond
 - Better integration of the financial audit and internal control audit
 - Additional PCAOB and SEC guidance that provides for a risk-based approach using reasoned risk and experience-based auditor judgments in areas such as rotation of testing and additional flexibility in using the work of others (similar to the approach in GAO's Financial Audit Manual).
 - Ongoing feedback from the PCAOB inspection process

Selected Federal Government Reporting Challenges

- **Financial and Performance Reporting**

- long-range fiscal challenges (e.g., per capita burden, sustainability, intergenerational impact)
- “trust funds” (e.g., restricted vs. unrestricted revenues, intra-governmental obligations)
- DOD assets, liabilities, and contingencies
- performance reporting
- Summary annual report

- **Audit Reporting**

- system of internal control
- financial vs. performance vs. other information
- Restatements
- Beyond “going concern” opinions (e.g., broken business model)

The Federal Financial Audit Environment

The federal financial audit environment is evolving:

- Closer to an opinion on the consolidated financial statements of the U.S. government (CFS), but DOD is the key challenge
- GAO, as the auditor of the CFS, needs to be able to use the work of the auditors of the agency financial statements
- Agencies need to meet accelerated due dates, maintain unqualified opinions, and address their internal control and financial management system deficiencies
- More timely financial and performance reporting should not come at the price of less reliable reporting

How Do We Move Forward?

- Good governance and accountability are critical
 - in the private sector to promote efficiency and effectiveness in the capital and credit markets, and overall economic growth, both domestically and internationally
 - in the public sector for the effective and credible functioning of a healthy democracy, and in fulfilling the government's responsibility to citizens and taxpayers
 - in both sectors to support a healthy economy that provides economic opportunities and benefits to citizens
- Sorting out the needs and effective and appropriate governance and accountability mechanisms for different sectors and types of organizations and on an international scale will be critical

Key Leadership Attributes for Success

- ***Courage***
- ***Integrity***
- ***Innovation***

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