

## DRAFT

### MEMORANDUM

ATTORNEY-CLIENT  
PRIVILEGED and CONFIDENTIAL

January 22, 1996

To: T. Jeremy Gunn

From: Laura Denk

Subject: Government Accountability Statutes

On December 6, 1995, the Review Board received from the Office of Management and Budget (OMB) a letter reminding all Federal entities of reporting requirements set forth in the Inspector General Act of 1978 and the Federal Managers' Financial Integrity Act. These two Acts, together with several other Federal statutes and OMB directives, subject Federal agencies to a maze of regulations concerning management of agency programs and operations. Unfortunately, the statutes and directives often overlap and rarely provide bright line rules for agencies to follow. This memorandum attempts to extract from the statutes and regulations the basic requirements that the Review Board must meet.

#### *I. Statutes at Issue*

- (1) *Inspector General Act of 1978*, as amended, 5 U.S.C. App. 3 (1978) ("IG Act")
- (2) *Federal Managers Financial Integrity Act of 1982*, 31 U.S.C. §§ 3512(b) through (e) ("FMFIA")
- (3) *Government Performance and Results Act, cite*, ("GPRA")
- (4) *Accounting and Auditing Act of 1950*, 31 U.S.C. § 3512(a) ("1950 Act")

In addition to these statutes, the Office of Management and Budget (OMB) has issued a number of directives to the heads of executive agencies on these issues, including OMB Circulars A-50 (Revised September 29, 1982), A-73 (Revised June 20, 1983), A-123 (Revised June 21, 1995), A-127 (Revised December 19, 1984), and A-134 (May 20, 1993).

#### *II. Summary of Concrete Requirements*

--IG Act: agencies must have audit and investigative activities (we should have audit activities)  
agencies must report annually on audit and investigative activities

--FMFIA: Federal managers must establish and maintain management controls (which should include an audit)  
agencies must report annually on management controls (can combine with above)

--GPRA

--1950 Act

### *III. Inspector General Act of 1978*

The IG Act requires Federal agencies to have independent reviews of programs and operations and to report annually on agency audit and investigative activities.

The Act requires two types of Government agencies to establish IGs offices: those agencies that have a Presidentially appointed statutory inspector general, and those entities that are “designated” Federal entities under the Act.<sup>1</sup> Under the IG Act, the Review Board qualifies as a “non-designated Federal entity”<sup>2</sup> which means that the Review Board need not establish an IG’s office, but it must report annually to OMB on audit and investigative activities. *Inspector General Act of 1978*, as amended, 5 U.S.C. App. 3 § 2.

Section 8G(2) of the IG Act requires the Review Board to submit a report to OMB and to each house of Congress by October 31 of each calendar year. The report must include the following: (A) a statement that the Review Board is not required to establish an inspector general’s office under the IG Act; (B) statements specifying the actions the Review Board has taken to ensure that audits are conducted of agency programs and operations<sup>3</sup>, including a statement that the Review Board has taken steps to ensure that the audit is conducted in accordance with Comptroller General’s standards; and (C) a summary of matters related to personnel, programs, and operations referred to prosecutive authorities, any preliminary investigations, and any prosecutions and convictions which have resulted. 5 U.S.C. App. 3 § 8G(2)(A) - (C).

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<sup>1</sup> “Designated” Federal entities (1) are regulatory agencies of the Government or (2) were established by the Government and receive over \$100 million annually in Federal funds.

<sup>2</sup>Section 8G(a)(1) of the IG Act includes “any other entity in the Executive branch of the Government” in its definition of the term “Federal entity.” 5 U.S.C.A. App. 3 (West Supp. 1994).

<sup>3</sup>Small agencies may meet the basic requirement for appropriate internal audit by obtaining audit services from an external authority, such as an existing office of inspector general. H. R. Rep. No. 771, 100th Cong., \_\_\_\_\_ Sess. 17 (1988).

Next year, the Review Board will also need to include any audit reports completed during the reporting period and a summary of any particularly significant findings. 5 U.S.C. App. 3 § 8G(2)(B).

The IG Act requires an annual *report*, but not an annual audit.<sup>4</sup> The FMFIA, explained below, grants Federal managers with discretion to determine a schedule for auditing activities.

#### *IV. Federal Manager's Financial Integrity Act*

##### *Statutory Requirements*

###### *Maintain Systems of Accounting and Internal Controls*

The FMFIA requires the head of the Review Board to “establish and maintain systems of accounting and internal controls that provide:”

- complete disclosure of the financial results of the agency's activities;
- financial information for management purposes;
- control over agency assets, *including internal audit*
- reliable accounting results that provide a basis for budget requests and budget control. The accounting results must meet the Comptroller General's audit and accounting standards. 31 U.S.C. § 3512(b) (*year/Supp.*)

###### *Internal Accounting and Administrative Controls*

Section (c) of the FMFIA requires Federal managers to establish *internal* accounting and administrative controls that reasonably ensure that:

- the Review Board's obligations and costs comply with applicable law;
- the agency protects its assets against waste, loss, unauthorized use, and misappropriation;
- the agency properly records and accounts for revenues and expenditures so that it controls assets and prepares reliable reports. 31 U.S.C. § 3512(c)

###### *Reporting Requirements*

Once the Review Board has audit results, § (d) of the FMFIA requires the Review Board to prepare a statement on whether its systems comply with § (c) above. If the audit reveals any “material weaknesses” in the Review Board's systems, the statement should mention the weaknesses and describe the agency's plans for corrective action. 31 U.S.C. § 3512(d)(2).

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<sup>4</sup>Cindy Salavantis in the Office of Federal Financial Management at OMB, confirmed that Federal agencies must *report* annually on audit activities. Federal law does not require agencies to conduct annual audits.

Section (d) also requires the Review Board to prepare a separate report on whether its accounting system conforms to the Comptroller General's standards. 31 U.S.C. § 3512(d)(2).

The head of the agency signs the statement and the report and mails it the President and Congress. Both the statement and the report will be available to the public unless information in the documents must be protected from disclosure by law. 31 U.S.C. § 3512(d)(3).

### *Maintaining Accounts*

Section (e) of the FMFIA requires the Review Board to maintain the accounts on an accrual basis to show the resources, liabilities, and costs of operations.

### ***OMB Guidance***

Two OMB Circulars, A-123 and A-127, discuss agency implementation of the FMFIA: OMB Circulars A-123 and A-127.

*OMB Circular A-123, "Management Accountability and Control" (June 21, 1995) (OMB Circular A-123).*

OMB Circular A-123 does not, unfortunately, provide Federal managers with much substantive guidance.<sup>5</sup> It contains sections on the GPRA, the FMFIA, the Chief Financial Officers Act, to which the Review Board is not subject, and the IG Act.

With regard to the FMFIA, the Circular states that the FMFIA covers more than fiscal integrity. "The Act encompasses program, operational, and administrative areas as well as accounting and financial management." OMB Circular A-123 at 4.

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<sup>5</sup>For example, section 3 is labeled "Actions Required." and reads as follows: Agencies and individual Federal managers must take systematic and proactive measures to (i) develop and implement appropriate, cost-effective management controls for results-oriented management; (ii) assess the adequacy of management controls in Federal programs and operations; (iii) identify needed improvements; (iv) take corresponding corrective active; and (v) report annually on management controls.

In extremely general terms, section II of the Circular defines management controls<sup>6</sup> and states that Federal agencies will develop management controls, consistent with standards listed in the circular, drawn largely from the Government Accounting Office's (GAO) "Standards for Internal Control in the Federal Government." Most of the standards are obvious:

General standards:

- programs must comply with applicable law;
- the agency must provide reasonable assurance that it safeguards assets against waste, loss, unauthorized use, and misappropriation;
- employees must have personal integrity, must be competent, and should communicate effectively within and between offices.

Specific standards:

- *Delegation of Authority and Organization.* The agency should have defined delegations of authority, designed to accomplish the agency's mission. The agency head should gear the organizational structure to effectively carry out the agency's mission.
- *Separation of Duties and Supervision.* Different individuals should authorize, process, record, and review official agency transactions. Managers should ensure that individuals do not exceed or abuse their authority.
- *Access to and Accountability for Resources.* Managers should ensure that only authorized individuals have access to resources and records.
- *Recording and Documentation.* Managers should ensure that the agency properly records, classifies, and accounts for all transactions.

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<sup>6</sup>The Circular states,

Management controls are the organization, policies, and procedures used by agencies to reasonably ensure that (i) programs achieve their intended results; (ii) resources are used consistent with agency mission; (iii) programs and resources are protected from waste, fraud, and mismanagement; (iv) laws and regulations are followed; and (v) reliable and timely information is obtained, maintained, reported and used for decision making.

Management controls, in the broadest sense, include the plan of organization, methods and procedures adopted by management to ensure that its goals are met . . . processes for planning, organizing, directing, and controlling program operations. A subset of management controls are the internal controls used to assure that there is prevention or timely detection of unauthorized acquisition, use, or disposition of the entity's assets.

- *Resolution of Audit Findings and Other Deficiencies.* Managers should evaluate and follow up on audit findings.

OMB Circular A-123 at 6-7.

Section III of the Circular describes how Federal managers should routinely assess management controls. In assessing the agency's management controls, Federal managers should use the following types of sources:

- management knowledge gained from the daily handling of agency operations;
- management reviews and program evaluations, including, but not limited to:
  - annual performance plans and reports pursuant to the GPRA,
  - reviews of systems and applications conducted under the Computer Security Act of 1987 and OMB Circular No. A-130, "Management of Federal Information Resources;"
- audit and investigative reports, including, but not limited to reviews of financial systems to determine if they meet the requirements of OMB Circular A-127;
- reports and other information provided by Congressional committees of jurisdiction.

OMB Circular A-123 at 8.

Importantly, OMB vests in managers the discretion to identify and implement the specific procedures necessary to ensure good management controls, and to determine how to evaluate the effectiveness of those controls. OMB Circular No. A-123 at 5.

*<to be edited and analyzed further>*

*OMB Circular A-127: Financial Management Systems*

*<insert requirements here.>*

### ***III. Government Performance and Results Act***

*<to be researched further>*

The GPRA requires agencies to "develop strategic plans, set performance goals, and report annually on actual performance compared to goals." OMB Circular A-123 at 3.

Managers should use such plans and goals in managing, budgeting, the budget process, and in reporting to the public on government efficiency and integrity. Id.

### ***IV. Accounting and Auditing Act of 1950***