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MEMORANDUM

ATTORNEY-CLIENT
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January 26, 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*, 5 U.S.C. § 306, 31 U.S.C. §§ 1101-1119, 9703, 9704

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. Threshold Issue: Whether the Review Board is Subject to the Accountability Laws

Each of the statutes at issue applies to executive branch agencies: (1) The IG Act applies to "Federal entities," including any entity in the Executive branch of the Government. 5 U.S.C. App. 3

§ 8G(a)(1). (2) The FMFIA applies to “executive agencies” and directs the “head of each executive agency” to comply with its provisions. 31 U.S.C. § 3512. (3) The GPRA applies to “agencies” and defines “agency” as “an Executive agency defined under [5 U.S.C.] section 105” and as “a department, agency, or instrumentality of the United States.” 31 U.S.C. § 1101. An explanatory note to section 1101 states that the term “agency” “is coextensive with and substituted for the term ‘department or establishment’ which was defined in 31:2 as in part meaning ‘any executive department, independent commission, board, bureau, office, agency, or other establishment of the Government, including any independent regulatory commission or board’.”

Congress conceived of the Review Board as an “independent” agency. According to the Senate Report, the Review Board is an “independent agency within the executive branch.” S. Rep. No. 102-328, 102d Cong., 2d Sess. 19 (1992) (“Senate Report”).

“[W]e must ask why the bill, which acts in the name of openness in Government, also exempts the Review Board from the Government in the Sunshine Act, the Freedom of Information [Act], the Administrative Procedures Act, and judicial review.” Senate Hearings at 3.

“On reflection, I think it would be best to amend the Joint Resolution to make the records of the Review Board itself subject to the FOIA and the Privacy Act, and to make the Board’s proceedings subject to the Sunshine Act and the Administrative Procedures Act. A law mandating increased Government openness should not itself establish an exception from general standards for accountability.” Senate Hearings at 21.

These passages can be read in one of two ways -- it shows that Congress recognized that it would be a burden for the review board to comply with all of the administrative regulations with which executive agencies must comply. But then Congress voted to make us be subject to these regulations. This either means that Congress intended us to be subject to all Government accountability laws and regulations, because we are an agency about accountability and openness, or it could mean that we are only to be subject to the openness laws listed above.

As a practical matter, it is very expensive for the Review Board to comply with these procedures. Federal Register publications alone are well

The argument that TJG makes is that the Board must be independent from the President’s influence. This is supported by legis. history:

“Remember, our intent is to establish a neutral body that gives legitimacy to our efforts. The very structure and appointment of the Board is designed to accomplish this by dispelling any notion of prejudice by any political persuasions or improprieties of any manner. Thus, it is imperative that the

review board be an independent agency.” Remarks of Rep. Stokes at the Senate Hearings at p. 28.

III. Brief Overview of the Statutes

- (1) IG Act
 - (a) *Primary objective:* To ensure that Federal agencies have independent reviews of agency programs and operations.
 - (b) *Reporting requirements:* Agencies must file annual reports to the President and Congress on agency audit and investigative activities. The report takes the form of a letter that agencies send to the President and Congress. It is due on October 31 of each calendar year.
- (2) FMFIA
 - (a) *Primary objective:* To require Federal managers to establish and maintain systems of accounting and management controls that meet Government-wide standards. The controls should include audits that cover programs, operations, and administrative areas as well as accounting and financial management.
 - (b) *Reporting requirements:* Agencies must report annually on agency accounting and management systems and state whether agency systems conform to Government-wide standards, as set forth by the Comptroller General and OMB in Circular Numbers A-123 and A-127. The report takes the form of a letter that agencies send to the President and to Congress. The report is due on December 31 of each calendar year. Agencies can combine their FMFIA reports with their IG Act reports.
- (3) GPRA

IV. 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.¹ Under the IG Act, the Review Board qualifies as a “non-designated Federal entity”² which means that the Review Board need not establish an IG’s office, but it must

¹ “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.

²Section 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).

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 operations³, 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).

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).

³Small 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).

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

V. Federal Manager's Financial Integrity Act

The FMFIA itself consists of four sections of 35 U.S.C. § 3512. OMB Circular No. A-123, "Management Accountability and Control" (June 21, 1995) ("Circular A-123"), provides agencies with additional guidance in interpreting sections b and c of the FMFIA.

A brief summary of the Act, followed by a summary of OMB's guidance, follows:

SECTION b: 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.*)

SECTION c: INTERNAL ACCOUNTING AND ADMINISTRATIVE CONTROLS

Federal managers need 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)

OMB GUIDANCE ON SECTIONS b and c OF FMFIA: OMB Circular No. A-123

Definition of Management Controls

⁴Cindy 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.

Circular A-123 defines management controls⁵ 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. They are listed below.

Standards (from OMB Circular A-123 at 6-7.)

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.

⁵"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.

Assessing Management Controls (from OMB Circular A-123 at 8)

Circular A-123 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; and reports and other information provided by Congressional committees of jurisdiction.

Identifying Deficiencies (from OMB Circular No. A-123 at 9-10)

Once the manager has assessed the agency's management controls, he or she should identify deficiencies. Certain deficiencies will be significant enough to report outside the agency in the annual Integrity Act report to the President and Congress. If a deficiency should be reported outside the agency, it is considered a "material weakness."⁶ Agency managers judge whether a weakness is significant enough to consider "material," but a manager should pay particular attention to an inspector general's opinion. OMB Circular A-123 at 9. The circular states that, "failure to report a known deficiency would reflect adversely on the agency." OMB Circular A-123 at 10.

Correcting Deficiencies (from OMB Circular No. A-123)

Once the Review Board has audit results, Circular A-123 requires agency managers to correct deficiencies in a timely and effective manner. (The IG Act specifically requires Federal agencies to follow up on audit findings.) OMB Circular A-123 at 10.

SECTION d: REPORTING REQUIREMENTS

Once the Review Board has audit results, it must prepare a statement on whether its systems comply with section c above. If the audit reveals any "material weaknesses" in the Review Board's systems,

⁶The term "material weakness" as used in the Circular has a different meaning than when Government auditors use it to identify management control weaknesses. According to the circular, auditors use the term to identify weaknesses at any level of the organization, even if the weakness should only be reported to the next level of management and not outside the agency.

the statement should mention the weaknesses and describe the agency's plans for corrective action. 31 U.S.C. § 3512(d)(2).

Section d also requires the Review Board to 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 then signs the statement and the report and sends it to 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).

OMB GUIDANCE ON SECTION d OF FMFIA: OMB Circular Nos. A-123 and A-127

Annual Report

Federal agencies should file their annual FMFIA reports by December 31 of each calendar year. Reports may be combined with the IG Act report and should be sent to (1) the President, (2) the President of the Senate, (3) the Speaker of the House, (4) the Director of OMB, (5) the Chairperson and Ranking Member of the Senate Committee on Governmental Affairs, (6) the Chairperson and Ranking Member of the House Committee on Government Reform and Oversight, (7) the relevant authorizing and appropriations committees and subcommittees, and (8) 10 copies to OMB's Office of Federal Financial Management, Management Integrity Branch.

The report should include the following information:

- (1) A statement of whether the agency can provide reasonable assurance that its management controls are achieving their intended objectives.
 - The agency head should make an informed judgment as to the overall adequacy and effectiveness of management controls within the agency. The agency head should consider information from the sources used to assess controls and information gathered from senior staff and the auditor.
 - Once the agency head makes an informed judgment, he or she should decide which of the three types of statements the agency should make to the President and Congress:
 - statement of assurance ;
 - qualified statement of assurance; or
 - statement of no assurance

The agency head should describe the basis for the type of assurance he or she provides, and describe the extent to which he or she assessed agency activities.

 - The agency head must sign the statement.
- (2) A report on material weaknesses.

- If the audit activities reveal any material weaknesses in agency programs or operations, the report should discuss agency plans to correct the weaknesses and discuss the progress the agency has made toward achieving those goals.
- (3) A statement on whether our financial management and accounting systems conform with Government-wide requirements. 31 U.S.C. § 3512(d)(2)(B).
- Financial systems should conform with the Comptroller General’s standards and OMB’s standards set forth in Circular No. A-127, discussed below.
 - If the agency does not conform with OMB standards, the statement must discuss the agency’s plans for coming into compliance.

SECTION e: 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 ON FMFIA: OMB Circular A-127, “Financial Management Systems”

The primary goal of Circular A-127 is to effect a more efficient use of Government resources by requiring each Federal entity to have only *one* integrated financial management system, thereby ensuring that data is entered only once, in the proper section of the system.

In large part, the Circular directs agencies to analyze financial systems and to create a five-year financial management plan based on the analysis. As the Review Board will not be in existence for five years, this section has little applicability to its operations.

The Circular prohibits Government agencies from spending Federal money on systems that do not meet the requirements of the Circular.

Objectives

Systems Operations

Agencies should use the best, acceptably priced, contemporary technology (e.g. software) for running financial system. The technology should be: (1) useful, so that the agency does not have more or less than it needs; (2) timely, so that it produces information as soon as practicable after the occurrence of the event; (3) reliable and complete, without being more detailed than necessary; (4) comparable and consistent over time; and (4) efficient and not “excessively costly.”

Systems Integrity

The financial management system should have reasonable management controls so

that it complies with OMB Circulars Nos. A-123 and A-71.

Support for Budgets and Management

The financial management system should be useful to managers in their budget activities, including preparing, analyzing, and executing a budget.⁷ The agency head should also design the system to meet the needs of program and administrative managers.

Required Actions

Financial Management System Directive

Agency heads should issue a “financial management system directive” and establish a “financial systems inventory.” The agency head should send the directive to OMB with annual updates to the list of existing and proposed financial systems making up the main system.

The directive should establish a single integrated financial management system, including a list of existing and proposed financial systems making up that system.

In the directive, the agency head should designate (1) a senior official to oversee the agency’s effort to review, improve, and report on the financial system, as the Circular requires; (2) designated system managers to ensure that each subsidiary system complies with the Circular; and (3) a senior audit official to perform audit functions, provide technical assistance and advice, and advise the agency head whether reviews of the financial management system comply with OMB Guidelines.

The directive should include policies to ensure that the agency is in compliance with the Circular. The following policies should be incorporated into the directive:

- managers who use financial information in making decisions should be involved in systems planning and evaluation;
- the agency should not spend money on financial systems, unless the systems comply with Federal law and OMB Guidance; and
- all systems that use financial management data shall acquire such data from financial systems in the inventory.

⁷See, OMB Circular Nos. A-11, “Preparation and Submission of Budget Estimates” and A-34, “Budget Execution.”

Annual Review of Agency Financial Systems

Financial system managers and users should conduct an annual review.⁸

Once the agency completes the review, it should:

- address all deficiencies; and
- use the review in creating the financial management plan.

Develop and Maintain an Agency Financial Management System Plan

The Circular envisions that each agency will develop a five-year plan for its system. The agency head should approve the plan and then submit the plan with the agency's budget request to OMB.

The plan should contain specific milestones and estimates. It should have a review and change approval process, and it should be coordinated with the information technology five year plan. [??]

Reporting

If the agency's financial management system meets the standards of OMB Circular No. A-127, then the system is acceptable for purposes of reporting under section (d)(2)(B) of the FMFIA.

VI. Government Performance and Results Act

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.

<to be researched further>

⁸In conducting the annual review, agencies should use the OMB Circular NO. A-123, as well as the OMB review guide: "Guidelines for Evaluating, Improving, and Reporting upon Financial Management/Accounting systems."

OMB Circular A-123 does not, unfortunately, provide Federal managers with much substantive guidance.⁹

A. Generally

1. FMFIA covers more than fiscal integrity

a. 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.

2. Managers have discretion to choose when and what

a. 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.

⁹For example, one section of the circular 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.