Testimony of
The Honorable Jack Martin
Chief Financial Officer, Department of Education,
before the
Committee on Government Reform
United States House of Representatives

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Financial Report of the United States Government for Fiscal Year 2004

Thank you, Mr. Chairman and Members of the Committee.

As the Chief Financial Officer (CFO) at the Department of Education, I am pleased to be here today to provide some perspective on the federal financial reporting process for fiscal year (FY) 2004. I look forward to sharing with you some observations on the Government Accountability Office's (GAO) report on the *Financial Report of the United States Government* ("Financial Report"), as well as the significant progress made by federal agencies during the past fiscal year.

Accelerated Financial Reporting

During this past fiscal year, the Federal Government achieved a significant milestone in the area of federal financial reporting. For FY 2004, 22 of 24 major agencies issued audited financial statements in their Performance and Accountability Reports (PARs) just 45 days after the end of the fiscal year. Prior to this year, agencies generally took up to five months to produce these same reports. Complying with an Administration requirement that took effect this past year, agencies have now significantly reduced the reporting delay that had been typical in the past. As a member of the CFO Council, where I have the opportunity to work with other agency CFOs and their deputies, I can tell you the entire CFO community is pleased and proud to have played a role in this major accomplishment.

The Department of Education was one of the 22 agencies that met the 45-day reporting deadline in FY 2004. In fact, Education met this accelerated deadline for the second year in a row, since we issued our 2003 PAR in mid-November the previous fiscal year – a year ahead of the requirement. Our success was certainly not attained overnight. Rather, the work done over the previous fiscal years, through careful planning and efficient execution, enabled us to reach this milestone.

For the two agencies that did not meet the 45-day accelerated deadline, the Department of Homeland Security (DHS) issued its PAR only four days after the 45-day period, while the Department of Health and Human Services (HHS) followed soon after in early December. The submissions by DHS and HHS should still be considered an accomplishment, as they came months earlier than was the norm in previous years.

The financial reporting efforts at the agency level enabled the Department of the Treasury (Treasury) to issue the government-wide *Financial Report* on December 15 for the first time. In previous years, the government-wide Financial Report was typically not issued until March. This accomplishment places the Federal Government financial reporting cycle on par with private-sector reporting.

With the accelerated reporting deadline taking effect this past year, agencies faced a one-year fiscal period in which there was less time to prepare audited financial statements compared to previous years. Despite this shorter reporting timeframe, a comparable number of Chief Financial Officers Act ("CFO Act") agencies received unqualified audit opinions on their financial statements in FY 2004 as in the prior year. Of the 24 major federal agencies, 18 received unqualified audit opinions in FY 2004. This result, in the face of a more rigorous audit schedule, is especially noteworthy since greater financial discipline and reliance on internal controls was needed to successfully meet the 45-day reporting timeframe. The accelerated schedule demanded good planning and timely reconciliations, and we are pleased with these efforts.

For FY 2004, I am pleased to report that the Department of Education was one of the 18 agencies that received an unqualified audit opinion. Education has received an unqualified opinion for each of the last three fiscal years, and we look forward to continuing this streak this year.

Some have questioned the accelerated reporting requirement, asserting that the earlier date may result in poorer quality data. From our perspective at Education, this is certainly not the case. Education has met this accelerated deadline for the past two years, receiving an unqualified audit opinion each time. And the unqualified opinion we have received has required a more rigorous financial reporting and audit schedule compared to previous years.

Further, the earlier reporting date has allowed our department and others the benefit of having financial information throughout the year in which daily management decisions can be made on a routine basis. The accelerated reporting requirement has driven process and control improvements that have laid the foundation for management reports such as Education's "Fast Facts." Fast Facts is a monthly reporting tool that highlights key financial and performance data in a consolidated and user-friendly format. Managers at the Department use Fast Facts to monitor performance and drive improved results in a variety of areas, including grants administration, financial metrics, and educational outcomes.

Among the agencies not receiving unqualified opinions, one agency – the Small Business Administration (SBA) – received a qualified opinion in FY 2004. Noteworthy progress is being made at SBA, as shown by its qualified opinion compared to its FY 2003 disclaimer of opinion. SBA's improvements over the past year have positioned it well for receiving an unqualified opinion in the future.

The remaining five agencies received disclaimers on their statements – DHS; the Departments of Defense, Housing and Urban Development and Justice; and the National Aeronautics and Space Administration. For several of these agencies, issues surfaced that could not be resolved in time to meet the accelerated reporting deadline.

(For additional information on federal financial reporting and financial management issues, please refer to the 2005 Federal Financial Management Report, which can be found at http://www.whitehouse.gov/omb/financial.)

Financial Report of the United States Government

In the government-wide *Financial Report*, GAO identified three main impediments to rendering an opinion:

- financial management problems at the Department of Defense (DoD);
- ineffective processes for preparing the consolidated financial statements; and
- deficiencies in accounting for intragovernmental transactions.

These three items were reported by GAO as material weaknesses in its report. All of these issues are complex long-term challenges and will take sustained efforts to resolve.

DoD is addressing specific weaknesses, and progress is being made. It is important to recognize that long-standing issues in a department that has over 300 sub-entities are not easily fixed. In some cases, eliminating DoD material weaknesses depends on the implementation of new financial management systems. In other cases, material weaknesses require an incremental approach to transforming business processes, which involves focusing on one component at a time or one financial statement line item at a time. Once a component entity determines that sufficient progress has been made, an independent auditor performs an assessment to ensure that the component is ready for audit.

For fiscal year 2004, the auditors determined that three significant financial statement items at the DoD-wide level – appropriations received, investments, and Federal Employment Compensation Act liabilities – passed audit scrutiny. In addition, six components, up from five the previous year, earned an unqualified opinion on their FY 2004 financial statements.

During this FY 2004 reporting cycle, significant progress was made in implementing a new process for preparing the *Financial Report*. The new process facilitates a stronger and more direct link to agency financial statements, something that has been a concern of GAO. While the new process was successful in producing government-wide financial statements within the new accelerated reporting time frame, there are issues that need to be refined and improved during FY 2005. The CFO Council looks forward to working with OMB, Treasury, and the other agencies to improve this process.

It is my understanding that the inability to balance significant amounts of intragovernmental transactions is being addressed on several fronts by OMB and Treasury. Process enhancements, such as more frequent reporting and reconciliation, and new tools like the Intragovernmental Reporting and Analysis System (IRAS), will support the efforts to eliminate reporting errors. These new analytical tools have helped to better focus corrective actions.

Internal Control

In December 2004, OMB issued the revised Circular A-123, *Management's Responsibility for Internal Control*. Circular A-123 defines management's responsibility for maintaining effective internal control and requires management to adhere to broadly accepted internal control standards and undertake a strengthened process when assessing internal control effectiveness. The strengthened assessment process is similar to the process that public corporations must follow under the financial reforms of the Sarbanes-Oxley Act of 2002. The policies contained in Circular A-123 further emphasize a foundation of disciplined accounting processes and good internal control for providing timely and reliable information and demonstrating financial accountability.

Eleven agencies restated their FY 2003 financial statements when issuing their FY 2004 reports. These restatements relate to a period prior to the implementation of the November 15 accelerated reporting requirement. Overall, the restatements reflect the greater scrutiny and attention the financial reporting process has received in recent years. Process and control improvements resulting from accelerated reporting and material weakness monitoring under the PMA scorecard, as well as the recent revisions to OMB Circular A-123 emphasizing internal control over financial reporting, will likely serve to reduce restatements in the future.

President's Management Agenda

One of my goals as a CFO is to produce more timely and reliable financial information, and to use this information in daily decision-making to reduce costs and better manage programs. These efforts are currently tracked by OMB as part of the Improved Financial Performance initiative of the President's Management Agenda (PMA).

I am pleased to report that the Department of Education has been in "green" status in the Improved Financial Performance initiative for just over a year. Education was the fourth federal agency – and the first cabinet agency – to reach this milestone, and several other agencies have joined us since then. Today, a total of eight federal agencies have received a green score on the PMA Improved Financial Performance scorecard. With the recent addition of the Departments of Commerce and State, eight agencies have an overall green status score – indicating that they have demonstrated they are using financial management information to manage their programs. I am further very pleased to report that the Department of Education received three prestigious financial

management awards during the last year: the President's Quality Award for Improved Financial Performance; the Certificate for Excellence in Accountability Reporting from the Association of Government Accountants; and the Alexander Hamilton Award for Technology (Silver) from the magazine "Treasury and Risk Management".

The Department of Education's success under the PMA and other financial management efforts is also shown by our receiving the Presidential Award for Management Excellence in 2004. I am pleased to report that the department was one of six agencies (selected from 61 nominations) to receive this award, which is the highest recognition bestowed by the government to federal agencies for management excellence.

A new program initiative of the PMA this fiscal year is the Eliminating Improper Payments initiative. Under this new PMA initiative, Education and 13 other federal agencies are taking steps to measure and eliminate their improper payments. These efforts include, but are not limited to, payments made in an incorrect amount, to an ineligible recipient, for a service not received, or for improper use of federal funds. FY 2004 began the first year of reporting under the Improper Payments Information Act (IPIA), and this information was included in the Department of Education's 2004 PAR.

From our perspective at the Department of Education, this first year of reporting is a vital step in meeting the objectives of the IPIA in that it establishes the baseline from which short- and long-term program-improvement strategies and priorities will be based. A focus of many of our strategies will be to improve the internal control surrounding these programs.

For information on the improper-payment-elimination efforts at other agencies, I would direct you to the OMB report, *Improving the Accuracy and Integrity of Government Payments*, which was issued in late January. (This report can be found at http://www.whitehouse.gov/omb/financial/fia_improper.html.) The OMB report provides an overview of what the CFO Act agencies reported in their PARs on their efforts to comply with the IPIA.

Conclusion

The outlook for the Federal Government to improve the quality and timeliness of financial reporting to the American citizen is positive. While many challenges remain, others that appeared similarly insurmountable just a few years ago are being solved. The Department of Education looks forward to working with OMB and the other agencies to improve federal financial management in the months and years ahead.

Thank you for listening. I am happy to answer any questions you may have.