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TABLE OF CONTENTS

Friday, October 9, 1998

A Financial Management Capability Framework for the Future
Hugh McRoberts, Office of the Auditor General of Canada

50 Years Progress of the U.S. Joint Financial Management Program: Much More to Do!
Karen Cleary Alderman, Executive Director,
Joint Financial Improvement Program, U.S.A.

Record Systems for Accountability: A Strategy for the Next 20 Years
Piers Cain, Director of Research and Development
The International Records Management Trust, London

Government Auditing: The Challenge of the Future

Moderator:
Kenneth Dye, President, Cowater, Inc., Former Auditor General of Canada
Panelists:
Dr. Mortimer A. Dittenhofer, Professor, Florida International University
I.P. Singh, Deputy Comptroller and Auditor General of India
Peter Armstrong, Technical-Administrative Director of the INTOSAI
Development Initiative (IDI) for the OLACEFS Region

The Annual Financial Report of the United States Government
Ron Longo, Senior Manager, KPMG Peat Marwick, Washington
Former Deputy to the CFO for Policy and Planning,
U.S. Treasury Department

Saturday, October 10, 1998

A Special Preview of the Future of Financial Management in the New City/State
The District of Columbia: An Overview

Dr. Abdusalam Omer, Deputy Chief Financial Officer for the Budget
The District of Columbia

Financing Local Government in the 21st Century

Tom Huestis, Deputy Chief Financial Officer for Finance and Treasurer
The District of Columbia

Taxing Local Government in the 21st Century

Natwar M. Gandhi, Deputy Chief Financial Officer for Tax and Revenue
The District of Columbia

Improving Local Government Financial Information in the 21st Century

Anthony Pompa, Deputy Chief Financial Officer for Financial Systems and
Controller, The District of Columbia

Information Technology for Local Government in the 21st Century

LaMont Wells, Chief Information Officer, The District of Columbia

Budgeting for Local Government in the 21st Century

Dr. Abdusalam Omer, Deputy Chief Financial Officer for the Budget
The District of Columbia

Managing Finances in the 21st Century City/State

Panelists:

Dr. Abdusalam Omer, Deputy Chief Financial Officer for the Budget
The District of Columbia
Natwar M. Gandhi, Deputy Chief Financial Officer for Tax and Revenue
The District of Columbia
Anthony Pompa, Deputy Chief Financial Officer for Financial Systems and
Controller, The District of Columbia
Tom Huestis, Deputy Chief Financial Officer for Finance and Treasurer
The District of Columbia
LaMont Wells, Chief Information Officer, The District of Columbia

The Current Global Financial Crisis: The Challenge Ahead

Jim Wesberry, Director, Americas' Accountability/Anti-Corruption Project
Casals & Associates

Opening Remarks

Jim Wesberry, Conference Chair
Director, Americas' Accountability/Anti-Corruption Project, Casals & Associates

James B. Durnil, President, ICGFM
President, National Rural Electric Cooperative Association

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The annual meetings of the World Bank and the International Monetary Fund have just adjourned, as some of you know, as the International Consortium's conference is held each year in parallel with this process. This year's conference is under the shadow of the world economic crisis, a crisis apparently much greater and much more serious than the debt crisis of 1983 and the decade of the 1980s. Today's newspaper, for example, says that the mood at the annual meetings of the Bank and the Fund was darker than a banker's suit. But I think our conference can be optimistic because, often, it is an economic crisis, a belt-tightening, an austerity period which causes and motivates reforms and improvements in financial management. That was true in Latin America after the Mexican debt crisis in the 1980s and 1990s, and we're going to discuss some of the reforms that were undertaken during this period at this conference. Looking toward the future, to the next 20 years, on this 20th anniversary of the International Consortium, we can be optimistic because we probably will have, even if there is a worldwide recession of the worst type, many opportunities to improve financial management which will be effective and efficient in the years after the recession.

I'd like to introduce to you now, James Durnil, the President of the Rural Electric Cooperative Association, and the President of the Consortium.

James B. Durnil, President, ICGFM
President, National Rural Electric Cooperative Association

On behalf of the International Consortium, I'd like to welcome you to our thirteenth annual meeting. This year, we are celebrating our 20th year, and we feel we have an exciting conference for you.

We plan to look at the past 20 years and what we have accomplished, and then look at the next 20 to give you some idea of where we feel we will be going. As in the past, the Consortium is pleased to team with the U.S. Agency for International Development, with the help of Casals & Associates, to provide you this year's conference. We also have some members of the private sector who are helping us with this conference. Specifically, we would like to recognize Price Waterhouse Coopers for sponsoring our Friday evening banquet. You might want to thank Ron Points during the conference for this sponsorship.

Our conference is for two and a half days, finishing at noon on Saturday. I think we have a strong program with some excellent speakers on private and public financial management. It is raining today, but we have a beautiful weekend planned for you, clear weather from Friday through Sunday. You may want to enjoy a fall evening in Washington, D.C. The hotel has offered a shuttle every five minutes to the subway station, so you can easily get to a downtown area.

At this point I would like to recognize two individuals on our Board of Directors. They are not only key players in our conferences, but also two of the founding fathers of the Consortium: Dr. Mortimer Dittenhofer from the Florida International University, who chairs our annual conference in Miami every March, and you have already met Jim Wesberry of Casals & Associates, who is responsible for this conference and who, I might say, has done an excellent job. Mort and Jim are the two original founders of the Consortium. I'd like to thank you both for guiding us through the last 20 years, and I'm sure you'll be around for the next 20.

In keeping with the electronic age, we are going to have all of the speakers' speeches transcribed and the questions and answers also recorded. A diskette will be mailed to all attendees, and it will also be posted on our Web site for you to download and print. So, to save a few trees, and to save a little weight on your trip home, you can get this material once you return home. It will make it easier for our recorders if you use the microphones in asking your questions. Please also give your name for identification purposes.

Again, in my judgment, we have organized an excellent conference with excellent speakers, and I'm sure you'll enjoy it. We have a social hour tonight at 6:00 p.m., so please come by and meet and greet our guests from overseas countries. I understand we have attendees from almost 30 countries here today. We've also organized a beautiful banquet for Friday evening and, as in the past, we have some excellent entertainment for your listening enjoyment.

The Consortium is pleased to have you here, and thank you for coming.

Keynote: Financial Management Reform in Guatemala

Jose Alejandro Arévalo
President, Central American Bank for Economic Integration
Former Finance Minister of the Republic of Guatemala

I'd like to first thank Jim Durnil, President of the Consortium, and Jim Wesberry, the Chairman of the event, for inviting me to open this event and tell you about the financial management system in Guatemala. Guatemala is a very small country, but a country which considers financial management very important.

First, I'd like to make a brief presentation about my country, Guatemala, for the 30 countries that are participating in this thirteenth conference, which is correctly called, 20/20 Vision, the Past and Next 20 Years of Governmental Financial Management. Guatemala is a country with a population of 11 million, located on the south border of Mexico. It is the first country south of Mexico in Central America with borders on El Salvador, Honduras and Belize. It has a gross national product of $17 billion and a growth rate of 5 percent. For 36 years we had an internal conflict which was finally over in 1996. Now, in Central America, and especially in Guatemala, we are democratic countries in a profound transformation process toward democracy and peace.

Now, I'd like to tell you about the integrated financial management system and the government audit system, a project which has been ongoing during the last three years by the Government of Guatemala. The Government of Guatemala is relatively small. There are about 170,000 government workers in the public sector, distributed in twelve ministries. The principal problem in this is the dispersion of financial information. This played a part in the inappropriate management of the public debt, resulting in an unfortunate increase in the public debt. Another serious problem occurred in cash management when, in the first month of our government, we were not able to pay the salaries of public employees. There was a chasm between budgeting and accounting and treasury. With this background information, I have some visual aids to show you which will help to explain Guatemala's innovative integrated financial system of today.

The system of financial management and control is part of the Guatemalan State which covers the following components: the integrated financial management system itself, the integrated management systems of the government, the national system of public investment, and the integrated system of government auditing. This final system is under the charge of the Controller General's Office. The first principle upon which this system is based is the principle of social auditing. Under this system, the public sector has a responsibility for control of results for the community and for accountability. Public services for the community are evaluated based upon principles of efficiency, effectiveness and economy, using measurements of quantity, quality and cost. We use either our own government personnel or contract specialized firms for purposes of evaluation. This system not only contemplates the community as a great user, but as the principal beneficiary of public services.

The objectives of SIAF-SAG are as follows: in the first place, the collection and effective utilization of public resources; secondly, timely and reliable information. It must be reliable to permit vigilance of the use of public resources by the community. For this to be possible, it is absolutely necessary that public management be transparent, and that each responsible public official is held accountable. For this system to succeed requires absolute integration between the financial administrative systems and the systems of control.

The platform we're using is an extensive use of computerized systems to obtain and process and report information, assuring that all the participants, whether they're within the public sector or outside the public sector, benefit by the information produced by the system. The system includes the operating units, the suppliers and contractors with the government, the banks and other collection agencies which collect State resources, vis-a-vis external participants. Internally, this system has three subsystems. First is the integrated financial management system, which is the one I'm going to talk about this morning. It encompasses budgeting, accounting, treasury, public credit and public investment. The companion subsystem, the system of public management, includes acquisitions and purchases, warehousing, State properties and property management, and human resources. And on the revenue side, we have the superintendency of tax administration, which is totally independent for purposes of tax levy and collection.

Now, I will refer to the integrated financial management system, SIAF. One characteristic of our financial management system prior to SIAF was the high concentration and centralization of the systems of budgeting, accounting and cash management. As a result, the Ministry of Public Finance became a bottleneck which interfered with the independency of all the other ministries. The integrated financial management system allowed us to decentralize financial management into the entities of the ministries of the government and the other autonomous entities, each of which is able to carry out its own affairs. This meant breaking a macrocultural system that had been in effect for more than 50 years.

In this culture, the principal resistance was within the Ministry of Finance itself. And, to a lesser extent, within the ministries themselves, because they had never had the responsibility for carrying out accounting, budgeting and cash management on their own behalf. So the first step was to set up a financial management unit within each ministry, and to select, train and prepare financial management personnel to administer the budget and financial management of each ministry. This was done last year in a planned program of training for the personnel of the financial management units and the ministries, in the independent organisms, and in the decentralized entities of the government. These are different sized entities. For example, the Education Ministry has 70,000 of the government's 170,000 employees. The Foreign Affairs Ministry has quite different characteristics with embassies and consulates throughout the world. The Ministry of Public Health has a whole network of public hospitals throughout the country, and part of the change is that now each hospital is responsible for its own financial management. In this way, the decentralization occurred first from the Ministry of Finance to the ministries, then moved out to the operating units of the different ministries and entities in the field level throughout the country.

As you will no doubt understand, a change of this type requires a change in the umbrella of legal administration a change of the laws. So we prepared and presented to the congress a new organic law of the budget, a new law for the Controller General's Office, a new law for probity and responsibility of public officials, and a new law for management of goods and services. The congress has already approved the organic law of the budget, which links together the decentralized authority to make decisions with the officials who are responsible for making the decisions and managing each entity.

What, then, is the information that this highly computerized system is presenting in Guatemala? It is based on a single entry of all data (all data is entered only one time) at its origin. It updates the information in the budget, accounting and cash management areas in such a way that we are able to prepare and execute the budget based on a single, unique database shared by all. Thus, we present information at different levels. First, at the institutional level, the lowest level, and the management level, so that each manager can access information at all levels. The Presidency of the Republic, the Finance Ministry, the Planning Ministry, the Sectorial Ministries each have different formats of information.

The SIAF covers the follow-on components to generate information for decision making. From the budget execution to the patrimonial accounting and treasury, it provides decision-making information to the central organisms and to management at all levels. At the same time, it provides accountability for the public. The follow-up and evaluation of any problems that might occur in the expenses and the resultant adjustment are done in real time so as not to skew the decision-making process. It is very important to point out that the system updates all the information, that is, the system is a system which is decentralized for making decisions even though it is centralized in regulation. From the point of view of a computer, the structure really is an Intranet for the Ministry and within each Ministry there is an Internet that is utilized for communication. In each of the different ministries, there is a small computer which is a parrot of the big computer in the Finance Ministry. The Health and Public Assistance Ministry handles 64 different hospitals, and each hospital handles, in an independent manner, their daily budget, accounting or treasury area, but is also connected on-line to the computer in the ministry. This computer, at the same time, is online with the Finance Ministry computer.

To implement this system, we used the Communications Ministry and the Transport and Public Works Ministry, and also the Health Ministry and Public Assistance Ministry for our pilot program. This year we have widened the system to six ministries. Next year we will integrate all 12 ministries in the government.

One can go into the system and one can easily analyze the data because it is a navigator-based system. We've developed a database which is very user-friendly. The software packages selected to develop the system were Oracle, Power Builder, Windows NT Server, Windows NT Workstation and Windows 95. We created a platform in which the one who requests the information can have access to absolutely all the information, depending on the security level of that person. Administrators of the system cannot change the data. However, they have access to all information in order to maintain the integrity of the system. If there are data problems or control problems, the appropriate parties are notified.

You can go into the system today on a daily basis to find out how your cash flow situation is doing or to determine if a proposed budget is sufficient to carry out the operations of each of the ministries. The system is structured in a generational database; it's a tree. It even allows access to the specific provider who had sold or supplied some tires, for example, for a vehicle, at a particular ministry, in one particular unit. This is in real time. In the past, processing the payment for the tire salesman required 139 different steps. This was reduced to three, and I believe that is still too many. Why? Because once treasury, budget and accounting are integrated, one has more efficient control.

This system generated some benefits for the Treasury Department. Before the system existed, if an entity requested $20 million, they got the funds and used them or they kept them idle. When the central government had a need for resources, they had to go out in the market to obtain these resources when within the system of the public treasury those resources existed, but they had already been assigned. We now have a dynamic, centralized manner of accessing information as to how much the entire government needs in terms of funds, when they're going to use it, and whether they can loan it from one ministry to the other. We can approve a loan to the Finance Ministry for 10 days because they need the money to pay salaries today, knowing the money will be coming in from taxes next week. This is one of the by-products or one of the advantages found by the financial administration in the integrated system.

Currently we have units of financial administration within each ministry. Before, each ministry sent requests for payment to Finance. Obviously, this created delays. Now each ministry does its own cash flow planning on a weekly basis. This cash flow plan is entered into the computer which allows us to plan sufficiently in advance the behavior of the income and outcome of the entire government, and the use of funds from a single cash fund.

There is now a process of editing the suppliers. This started within the Finance Ministry. We don't use checks anymore; we don't make payments by check. This is done through electronic transfers. The average payment is made within 48 hours.

A computer system of this size can be controlled completely if the controls are incorporated from the very beginning, This system views not only the needs of the administration but also the needs of auditing. SIAF-SAG places as much importance on the controls in the system as in the design, analysis and programming, and implementation of the system. To implement the system, it was necessary to reorganize the Controller's Office, because they had not used an integral, unified, on-line system before. Now they are able to do complete, on-line, real-time auditing with their own computers. Also, since each ministry has its own unit for financial management, internal auditing units were created within each ministry, but they don't report to the minister. They report, rather, to the General Controller of the country.

What are the contributions of this system? The first one is timely information. Timely information in real-time is now being executed and very timely decisions are being made throughout the ministries. The second advantage is that the information is coherent and dependable. In January of 1996, I asked the Treasurer about a certain figure on the internal debt. One gentleman gave me one piece of data and the Treasurer gave me another one. It was very difficult to determine which figure was correct. If I had asked the Controller, I would have gotten yet another answer. The ministries had to make a lot of decisions this way in the first year. Certainly we made a lot of errors because the system was not integrated. Each one handled information differently with different criteria and different concepts. The third contribution of the system is the ability to measure the capacity of each one of the ministries as a public manager. Before this system was in place, the Minister of Communications, Transportation and Public Works, in infrastructure, could perfectly well say to the President, We could not build a certain road because it is the Financial Minister's fault. Using the example mentioned before, a decision is made to pay a supplier for some tires. The decision was not with the person who had the problem, the Director of a hospital, but with some employee within the Ministry of Finance who was completely ignorant about the situation in the hospital. So we couldn't buy new tires and the ambulance couldn't go because no one knew what was going on. This was multiplied by thousands of different situations.

As we work with this system, control is taken by each one of the different offices and institutions and ministries. This has permitted the President of the country and the ministers and the chiefs and the bosses to control the work according to the results. How are they handling the budget? How are they managing the work plans? It also makes it possible to know, unlike in the past, the various costs involved in the public services that are granted.

A very important element of the system is the transparency in the administration of resources. I asked journalists from the entire country to come and monitor how the public resources were being handled. To give you an example, some journalists began to scrutinize where the Ministry of Defense was spending its money. They looked at the Ministry of Health. Any citizen can search through and navigate the system to find out what purchase order generated a specific payment who is paid, what is paid, and what service has been rendered. If the citizen wants to, he can ask how many goods and services this particular supplier has provided to the government in all the different ministries.

All of this has also permitted us to have a huge reengineering in our administrative processes. At the beginning, there was a lot of resistance. People thought they were going to lose their jobs. We assured them that what we were changing was the quality of the personnel. The number of people working was the same. But for this kind of analysis, we wanted to have professionals well prepared in financial management. So we replaced some of the old workers for new ones, different ones, who were able to work with the system.

This has permitted us to move ahead in a significant way. The Ministry of Finance, where information and decisions were concentrated, is where corruption was the worst, where it really started in the Guatemalan Republic. This is where decisions were made about who would be paid, who wouldn't be paid, what contracts would be carried out, and which ones would not. This concentration of power has passed through a process of decentralization in which the public managers are responsible for their own resources. They have the authority to use these resources. Also, discretionality is being changed. There is now limitation of specific responsibilities for each person, each unit.

The struggle against corruption is not only involved in decisions for contracting and payment. It also occurs in the improper collection of favors by employees dealing with specific suppliers. A supplier used to pay money under the table to a certain employee so his payment could be received without delay. With 139 different steps, each one of these people might ask for something to make the thing go smoother. Now the computer eliminates these practices. The opportunity for corruption has become a very simple administrative process with greater transparency. We now have a community that is well informed about what's happening with their resources.

What are the successes of the system? Where are we now? It is a system that is in the process of being completed. We are now into the second phase. The successes up to now are that we have been able to deregulate the legal structure and move onto a more modern structure. We've accomplished a deconcentration of expenses, an ordaining of the budgetary execution, and the coordination and interdependence of the different leadership organizations' budget, acquisitions, purchasing, etc. Also, we've eliminated discretionality. We've improved transparency in the obtaining and use of resources. We've had timely information that is also dependable and in real time.

There are now modules functioning in treasury, accounting and budgeting. We're working on the public credit. SIAD is working on purchasing, warehousing, goods of the State and human resources. We're busy installing a new tax system approved in January of this year.

I would like to point out that this kind of project, SIAF-SAG, requires political support. This is perhaps the most important requirement because these projects should be seen at a medium and long-range view. To install a system of this type, you face at least three major challenges. The first one is change of culture, changing the mentality of the employees or the public workers. This requires training, education, and also requires the authority to carry out the changes. It requires political decision at the highest level, that is, the President of the country himself, along with the political forces, must be able to move ahead in the face of powerful resistence beginning with the corruption which is involved profoundly in the public sector. This change in conduct and mentality is most important. The second challenge has to do with the education and use of technology to serve the community. We develop computer systems in order to use them. If people don't know how to use them, it makes no sense to implement them. The third challenge is to reeducate, and this is very important, to reeducate the decision makers within the public sector. Because governments never had this information before, they don't realize the importance of the information in decision making. It may be that the information, even though it is available, is not being used by those who are making decisions, starting with the President.

The private sector has supported this initiative. This is the largest accounting system of Guatemala, and the budget of Guatemala is small, but we're still talking about $2,500,000. For 170,000 employees, this is an integrated, on-line, real time accounting system. It is the largest system in the country functioning in a decentralized fashion.

To conclude, the system of financial administration is a system for making decisions in control, but especially it is a system to reeducate public servants, linking accounting information with results. The people who are involved in financing are tied to the accounting system, and those who are responsible for the finances of the country are obligated to face the public in ensuring the proper handling of public resources. By having this information available on line in real time, we have details down to when you paid the last transaction, every little transfer, etc. It's the best control that society can have. This kind of system, I want to tell you, has many enemies. During the entire process, I can assure you that we had, and still have, a lot of pressure, because there are many people who don't like to have this kind of information available in this level of detail and available to all of society.

Thank you very much for your patience and attention. I'm available if you have any questions.

MR. WESBERRY (United States): We're very pleased to have a Finance Minister capable of doing a presentation on very technical material as was done here today. I'd like to take this opportunity to ask if you can tell us a little bit about the Central American Bank for Economic Development.

MR. ARÉVALO: Thank you. I am very grateful to have this opportunity to share with you briefly information about the Central American Bank for Economic Development. It was created in 1960 by the Central American government. Its main objective is to promote the process of economic integration in the Central American region. I have the privilege to direct this organization right now. It is an institution that handles $2.8 billion and a portfolio of $1.9 billion, of which one-third is a project from the private sector and two-thirds are projects from the public sector. We utilize close to 85 different private and public banks within Central America as a go-between, and we also work with projects directly with a capital of around $960 million. This tells you very quickly what the Central American Development Bank is.

MR. DECENO-LUGO (Dominican Republic): I ask this question because, in your presentation, you used the term vigilance. And perhaps my question is based on the task that is being carried out in the Dominican Republic by the organization over which I preside. You said, I believe, that all of this is from the point of view of administration, but how can the people in Guatemala find out how public resources are being handled? You said that they can find out through the Internet. What if they don't have the Internet? The other question is, does the Congress in Guatemala have access to the information? Do they intervene and watch that this is done properly?

MR. ARÉVALO: I shall try and answer your question. Both are basically connected because Congress represents the people. The communication of the task carried out by the Finance Ministry with the Treasury Department through written communication systems, in my opinion, is essential. There is an obligation from the Finance Ministry to inform the people about our resources. For the three years in which I was the Minister, every Friday at 11:00 in the morning the newspaper people would come and gather with me. We had a press conference and we would inform them, even though the system was not yet installed, about the use and obtaining resources through taxes and the use of the public resources. This was an important process because, unfortunately, the government of my country had lost the public trust. Heretofore, the Guatemalan government had not made an effort to inform the people, week by week, of how we were utilizing our resources. Now they can monitor. This is the only way of recovering that trust that was lost through decades. On the other hand, the Congress of the Republic has two basic mechanisms: A Finance and Currency Commission that does the job of supervising the differing activities of the Finance Ministry and the other is the Probity and Responsibility Commission. They have access to these systems. They have access to the technology. In order to reach the public in general, the only way that we have found is telling them on a weekly basis what the government is doing with the resources or the public funds. This is mainly directed to the economic analysts who also have access through the Internet. Obviously, along with our government itself, there are newspaper people who also utilize this technology, and you can be sure you don’t need to point out this information to the political opposition. But it is not oriented to the great masses of the people. For that, it is important to utilize the media, the social communication media, through the press. But through the Internet, journalists, economic analysts or the different parties in opposition to the government can corroborate what the Minister is saying in a direct manner. In other words, it provides more transparency and more confidence in the way the government is comporting itself.

Finally, I want to refer to the Accounting Office. For some strange reason, the General Accounting Office and the different entities responsible for supervision of fiscalization are very weak. The Controller’s Offices are very weak in Latin America. They are not independent in general. I can talk about what happens in my country. In order to implement appropriate and necessary government auditing, it was essential to institute a very deep, profound reform in the Controller’s office. They can utilize that technology to analyze a situation and change the way things are done. They know very quickly the use or misuse of public funds. Therefore, the computer system becomes an ally of the Controller, so long as the Controller is willing to make the effort and the sacrifice necessary to participate in all this. For my country, I thought that it was essential that the Controller participated from the beginning in the design and utilization of this system.

MR. PORTILLO (El Salvador): You mentioned the words follow-up and evaluation. I would like to know who does this follow-up and evaluation and whether there is any organization in particular that does the follow-up work for SIAF.

MR. ARÉVALO: There has been follow-up on the implementation of the system, and there is a follow-up also on the execution of the government process. Each week the Controller's Office as well as the Finance Ministry and the different SIAF units have the obligation to do follow-up work on the system. Each week they would let me know exactly how they changed the documentation and how we were meeting the implementation plan for this system. Each month I would meet with the Controller. We headed the follow-up effort. We made decisions and took corrective measures when problems arose. The decisions made with the Controller’s Office required considerable integration and harmony. I would like to thank the Controller publicly for his valuable participation. The ministries themselves had to become involved. This cannot be delegated. Of course, one does not get into the detail of it, but one has to be behind every system, moving whatever has to be moved, throwing off the opposition, changing criteria that has to be changed, and confronting the natural resistance we human beings have to change. There has to be a political commitment at the highest level.

Government Financial Management:
20th Century Achievements, 21st Century Challenges

Maurice C. Mould, Former Senior Adviser, The World Bank
Former Secretary General of the ICGFM

I was minding my own business and the government's business in Moscow last week, when I get, through the Internet, a message from Jim Wesberry. Can you give a paper? That was the last thing I wanted to hear about in Moscow at that particular time. But, as he has been a good friend of mine for a number of years, and I owe him, I decided I would give a paper.

When I got in today, the first question was, Can we have your paper? And I said, Well, I don't have one. I've got some notes and I'm going to talk from these notes for a little while. I can make it as long or as short as you like. Jim says, Keep it light and keep it short. So I'm going to try to do that.

These days I'm fortunate. I live in Texas. Texas has a wonderful crop of bumper stickers. One of my favorites is, Do not steal. The government hates competition.

Jim wants me to talk about the achievements of the 20th century. Well, I'm not the oldest person in this room, but I've got few competitors. I've seen much of this century, and some of the financial management or lack of it in governments. But I think the first credits must go to governments, because as the 20th century has evolved, governments of all shapes and sizes have taken on increasing responsibilities for their peoples. And this, in turn, has had the follow-on, knock-on effect of requiring better, improved financial management to achieve certain levels of accountability.

When you look back to the beginning of the 20th century, it is surprising to find how few effective managed governments there were. There were an awful lot of colonial governments which really weren't set up to manage the affairs of their people much more to keep track of what went back to the colonial powers much more to achieve law and order and keep the local people in their place. And so it wasn't until after World War II that we saw the real growth of new governments, and new governments that needed financial management systems. Many of them soldiered on with the old colonial systems for quite a long time. Some of them still do. I'm sure my friends from India would admit that the system they use today isn't far removed from the one they took over in 1947. But these systems, as they have developed, have supported massive changes in the welfare of people. I think that those many accountants, financial assistants and budget assistants who labored long for very, very little pay should be congratulated for bringing their governments to the state of financial management that we find today. Sure, it's not perfect today, but it is a lot better than it was.

Some of the more difficult ones to put right at this stage are those in the command economies, or which were command economies. They present considerable problems as yet. But I have no doubt that even these will consistently improve their financial management. China, for example, is taking massive steps. It has massive problems to overcome. At the present time, the Ministry of Finance in China has released five accounting standards in harmony with international standards. It has another 20 it proposes to release in the next two years. I'm going to China next week to work with the government and the World Bank to develop another 17 accounting standards in harmony with international accounting standards. That's going to be 42 accounting standards in China, which will take them over into the next millennium. Not bad for a command economy.

Russia is a little slower. I was in Russia last week, and life was a little difficult. Not for me, it was easy for me. It really is difficult for the people in Russia, because their financial management systems don't work. They really are in trouble. But, they'll get out of it. They have one of the better educational systems for people in the world. It is just that, in the command economy, priorities are misaligned. What they have to do now is to get them better aligned toward better financial management.

I'm trying to look on the bright side, but still there are problems in the 20th century systems. Many government systems today are still too inflexible. They are still running down straight runway lines or tram lines. They are not yet attuned to using databases and taking information from those databases for whatever purpose they need. I'm continually seeing World Bank projects in trouble today because the financial information does not flow effectively. Sure, it is all there in the government system, but to get it from the government system into the World Bank form of reports still is an art form, because the government systems remain inflexible. There is still a lack of management accounting. There is still much too much focus on, Let's spend the budget and account for spending the budget. Listen, if we don't spend our budget this year we won't get the money next year. So we must have the money, and we're going to account for spending that money not how it was spent, particularly, or whether it was spent well, but just show that we spent it. Management accounting systems are coming into governments. Certainly into the more sophisticated governments. But I can count the more sophisticated governments on my fingers and toes. Twenty. After that, there are about 157 that are not very good. But a number are getting better. Our job, moving into the next millennium, is to make them better.

There are some strong underpinnings which have taken place in the 20th century, particularly the last 20 years of the 20th century. We have seen a very strong development of INTOSAI. INTOSAI, the Organization of Supreme Audit Institutions, has grown from a very tentative infancy to a very strong organization. Unfortunately, it still has its political underpinnings which make it difficult for some Auditors General to be effective. Please don't criticize all those Auditors General. I've criticized them, but think again. Most of them must have some form of political support to get there. Despite that, they have succeeded in moving away from the traditional compliance audit in many cases to more effective, efficient audits. Led, encouraged, by the more sophisticated audit organizations from Canada, and I can see Ken Dye smiling there in the audience, and by the audit organizations from the United States and the United Kingdom. These three countries in particular have offered a lot to organizations such as INTOSAI and encouraged the International Federation of Accountants (IFAC) to become far more active in the public sector and public sector accounting. There has been a growing trend in the United States, through IFAC, to establish public sector accounting standards. Very sound underpinnings, which can help take government accounting into the next millennium.

The Controller General of the United States and the Auditor General of Canada, one Kenneth Dye, joined together to start examining the utility of producing annual financial statements of government. This initiative has taken seed with a number of governments now. I think Ken would agree, and Mr. Bowsher would agree, that the first ones left a little to be desired. Nevertheless, they started. They made an effort. It is always going to be difficult to produce a set of financial statements for a government. No government likes to have somebody counting its tanks and aircraft. No government likes to be told that it hasn't got a funded pension liability. But these are all good starting steps. New Zealand and Australia have started. If anybody has not seen New Zealand's financial statements, they're worth a look.

One of the things that the joint American-Canadian team did was to examine who were the users of government financial statements. This, I found to be very, very interesting. I think all governments should find out who is using their financial statements. It is worth reading the reports that have been developed and are being developed by the US and Canada. But we have to move on from these youthful underpinnings and be aware that more entrepreneurial-type activities of government are being used by the private sector in many parts of the world. We went through the phase of nationalization to privatization. It has been interesting to watch how quickly and effectively some countries can achieve privatization because the accounting which was taking place under nationalization was very effective. It was quite easy in some countries to measure or to forecast the likely performance of utilities which were being put up for sale. The government accountants who had been responsible for running the finances of these organizations should be congratulated. I can also give you a number of others that ought to be led out to the slaughterhouse, because the information they offered when the governments tried to sell those organizations was useless. The government had to spend very large fees to encourage the Big Six accounting firms to come in and do a complete recast. But it was not all doom and gloom. A number of very useful sets of financial statements and financial supporting information have been made available to governments.

Let me leave the 20th century on one rather unhappy note, and, that is, I still see too many governments using the employment of staff as a social security system. That tells me very quickly that the financial management of that particular government is not very good, because they clearly are not measuring the performance. They don't want to measure it, because they're hiring their sisters, brothers, cousins and aunts. It is still going on. It is not limited to developing countries. It also happens in developed countries.

Now, for the coming millennium, what are the challenges we face? One of the challenges undoubtedly is going to be information management. We still have too many managers in governments that don't understand information management, don't understand computers. We still have the chief accountant who wanders over to one of his juniors and says, Can you copy the Internet on this diskette for me please? The challenge of the 21st century is going to be information management. I believe that information management will in effect replace the accountant as we know him or her.

I have noted for a number of years that what I learned to qualify me as a financial consultant is not very material today. Nobody taught me Excel when I qualified, but I'd better know Excel now or I don't survive as a consultant. About the only useful thing left from my training is that you have to have a debit to match a credit, and a credit to match a debit. After that, forget it. You're into new territory. One of the first steps you're going to have to take when the Year 2000 comes along is to make sure that your computer recognizes the Year 2000. For those of you who have not looked at your computers and your software to be sure that it will deal with 2000 and not return you back to the beginning of the 20th century, 1900, you'd better start looking. That's your first challenge for the 21st century.

The next challenge is going to be accountability and the politicians. I hear people complain all the time about government accounting and government financial management. They accuse financial managers in government of the worst dereliction of duty. It is not easy to be a financial manager in government. It is much easier to be the financial manager of Proctor and Gamble. It is much easier to be the financial manager of Dell Corporation or Microsoft. You know exactly who you're dealing with and exactly what their objectives are. But objectives in the life of a politician vary week by week. Trying to financially manage isn't easy. The Italians, I think, have got politics sewn up better than most. You know how to spell politics, P-O-L-I-T-I-C-S, right? The P-O-L-I in Latin means little. T-I-C-S means small, biting insects. And so politics are small, biting, blood-sucking insects. Not a bad description, sometimes.

Politicians still do not effectively recognize that you only get what you pay for. Government staffs around the world continue to be underpaid. As a result, there is over-employment and under-efficiency. No amount of financial management efforts on the part of government financial managers can change this very quickly. So that is a challenge for this coming millennium how to get what you pay for efficiently, expeditiously, accurately, and end up with a happy band of government workers.

Whenever I come to Washington, I ride on the Metro. I know that on that Metro train probably 40 percent of the riders, maybe more, are government workers. I look at their unsmiling faces. I look at their unhappy states. I worked in government. I know what it's like. You can have fun in government. But it's not easy. Therefore, I would like to see in the Year 2000 onwards, an effort by the politicians and the people that work for them to reach a better compromise on the employment conditions for government workers, and particularly, government financial management workers.

I see continuing, mounting pressures for containing costs and measuring costs, measuring performance. That is going to grow, and it is going to be able to grow as more and more databases become available, more and more information management techniques become available. But those databases will in fact change the way in which accounting, as we have known it in the 20th century, takes place. There will be much more measurement by statistics rather than measurement by balance sheet. Incidentally, I think balance sheets will disappear, but that is just another personal opinion. I'm not talking just about government ones. I'm talking about balance sheets across the whole spectrum of accounting. That's something for another session.

I think there will be international or regionally international standards of measurement. The coming of the EQ in Europe is going to bring about performance measurement within those governments that are contributing members of the EQ. Once we see that grouping become successful, and I believe it can, then we are going to see more groupings. There is a grouping already on this continent Canada, United States and Mexico. But it is still tentative and it is not yet formed properly, but I think it will be. I think you're going to see standard, common methods of measurement of performance developed in that region. It's only going to take 30-50 years before these regionals become internationals. Already in the 20th century we have seen the movements toward international accounting standards. We're going to look for international performance measurement standards.

Computers have changed all of our lives, and they're going to continue to do so. I find it difficult to forecast exactly where they are going to end up based on the changes which they have wrought in the last 20 years. We're entering this next century with a range of computers and software which was unimaginable 20 years ago. So there will be new computers and new software. Or, if Bill Gates does his job, maybe something entirely different which we will have to learn all over again. Maybe you will and maybe I won't.

I think we're going to see much more mobility between the private sector and government in terms of moving expertise about. One fact I ought to mention regarding the 20th century was the willingness of a number of governments to take onboard temporarily or for quite long spells the expertise of accounting and management consulting firms. That's not just limited to the more sophisticated 20, but many of the developing countries have been willing to take on this expertise. I think, as you move into the next century, there will be an increasing exchange. I think the lines between the private and public sector, so far as information management is concerned, will be very blurred. People will move much more rapidly from one to the other, particularly if we can get the price right.

I don't think there will be any more pension systems in government; I think governments are already concerned about the liabilities that they've built up. That is going to increase mobility of individuals between the sectors. No longer will people be tied to the pension umbilical cord.

Already, as we move into the next century, the major accounting organizations, which started out as the Big Ten, changed to the Big Eight, Big Six, Big Four, Big What? Those of you who are members of the Big Four here today probably won't agree with me, but I think you are going to see a break-up of all of that at some stage. It will become, I think, a much more regional and international organization. You say, Yes, we already have the international organizations. Yes. They are on the top tier, but locally they still work very much on their own. I think as we move into the early years of the next century we are going to see significant changes. Not only in the way accounting firms join together, I think we're going to see something which this body, the International Consortium, has long sought, and that is international groupings. I think we will see much more international groupings of government accountants. INTOSAI has a truly international operation. I think you're going to see the Consortium moving much more steadily that way, but it can only happen if you agree to it. You, in this room, are the only people that can make it happen. So get some young people and encourage them to go out and do some missionary work.

I leave you with the problem of accountability. That is going to haunt you, haunt us, well into this next century. How to achieve meaningful accountability, not just of public funds, but of funds of any organization. Many of the big companies, many of the small companies, do not really achieve effective accountability.

At this particular point, I just want to leave you with a couple of thoughts. You've probably seen in various magazines and what have you the terminology Only in America. I've got one or two for you here. Only in Moscow can you get a pizza before you can get an ambulance. Only in Canada are there handicapped parking places in front of a skating rink. Only in America do people order double cheeseburgers, a large fry and a diet Coke. Only in England do the banks leave the doors wide open and chain the pens to the desks. Only in Germany do they leave their Mercedes in the driveway and store all their useless things in the garage. Only in Japan do they use answering machines to screen calls and then have call waiting so they don't miss a call from someone they didn't want to speak to in the first place. Only in America do we buy hotdogs in packages of ten and buns in packages of eight. With that, folks, that simple accounting exercise, I will leave you. Thank you for bearing with me and listening to me. It has been a pleasure to talk to you again. Thank you.

MR. EINHORN (United States): Do you have any thoughts on the problems of universities?

MR. MOULD: Raymond, you have hit on a great omission on my part. I really ought to pay tribute to the work of the universities, not just for producing accounting experts for the public sector, but also for the private sector. One of my proud boasts is I have only been to a university to teach. When I was a youngster, we couldn't go to the university. Since I graduated, by correspondence courses, the universities have expanded their accounting training, their auditing training, not just in the

United States or in Europe, but in many other countries like Kenya, Malaysia, Thailand and Russia. The universities have done an excellent job, and I cannot see any reason why they should not go on doing that into the next century.

MR. DESTA (Ethiopia): What will be the accountability problems as it relates to the increase of corruption in the 21st century?

MR. MOULD: I challenge you, sir. You said it is on the increase. What are your grounds for such a statement? It has been around for a long, long time. I used to be able to quote passages from the Bible on this, but my old age is beginning to tell on me. It's been around, and it isn't going to go away. What accountants and auditors have tried to do, and in many cases have done successfully, is to ring fence it. I think that is what we have to do, keep ring-fencing it, and slowly whittling away at it. But, remember, particularly those of you in government, that politics today are high finance. Politicians can only get into office by the use of high finance and, inevitably, something spins off, rubs off, somewhere. I'm not criticizing them for this. This is a fact of life. It is the only way they can become politicians. What the accounting profession has to try to do is to keep opportunities for corruption to an absolute minimum, to publicize it wherever it is discovered, and use techniques ranging from simplistic internal controls to much more sophisticated controls which you can engage through local law enforcement authorities. Ring fence it. You will not stop it. If you stop it, it is going to be a perfect world. I don't think it's ever going to be a perfect world.

MR. ENTHOVEN (United States): Maurice, may I hook onto what Ray asked about education? For public sector financial management, what do you see in the next century or even the century thereafter? How will the training be most effectively carried out around the world in the public sector? We in the university, unfortunately, are lagging somewhat behind in trends.

MR. MOULD: Computers, Adolf. Computers. You're going to see the development of interactive software packages which enable people to learn either singly or in groups. A person can learn to play table tennis on an interactive screen with nobody playing with him, just the screen and the ball apparently coming backwards and forwards as he strikes at it. When he strikes it correctly, he gets marks, and when he strikes it incorrectly, he gets deductions. That is just one example of interactive media that is available today.

I think that the big firms will find that this interactive media will be a much less expensive form of training. And it is capable of being changed very easily. You will have your information systems manager asking the information technology person to tweak this, tweak that, change this, change that. Before you know it, you've got a new system which can teach somebody the very latest developments. The airline industry did this a long time ago with flight simulators. The accounting industry has been very slow to catch onto this, but it is coming. Not only will the big firms do it, I think you in the universities will start using this as a training technique. It can work for individuals, it can work for groups of people, and it can work not only in Washington D.C. You can have the set-up in Washington, D.C. and you can operate it in 50 cities around the U.S. or 50 cities around the world.

MS. ROBINSON (United States): Maurice, the Consortium and Transparency International and other internationally focused organizations place a lot of emphasis on ethics and transparency in the hopes that we'll see diminution of corruption. Do you see major changes in corruption in governments around the world in the next century? And if you do see it, what do you think will bring it about?

MR. MOULD: Ring fencing will bring it about. What's going to happen is you'll ring fence a problem there and somebody will find a way to do it over here. So you're going to have to go over and ring fence that problem. Corruption won't stop. It's going to be, and has been endemic in society for thousands of years. You're not going to stop it. All you're going to do is move it from one place to another. I can't offer you wonderful, hopeful ideas on how you're going to stop it. If people want to buy somebody, and they've got the money to do it, they will do it. And they will find all sorts of surreptitious means of doing it. It is unfortunate, but I'm afraid if people want something badly enough, there is a price for still too many people around this world. One of the things that can help to ameliorate it to some extent is pay people the right price in the first place. Too many people, particularly in the public sector, are underpaid.

MR. DURNIL (United States): You know, in that light, I run a company now, and I don't know how many government employees I've got on my payroll around the world, but some people call it salary supplements and some call it holiday pay. Some development banks, the World Bank, consider salary supplements to be a normal cost of doing business. In the United States they may call that bribes. Do you have any comments on that?

MR. MOULD: You quoted the World Bank and the payment of salary supplements. I've long had two minds about this, but in the end I've come to recognize that if you want the job done in a particular country, you are unlikely to get it done at the local price. You want to get it done expeditiously, because by getting it done expeditiously you're going to benefit a lot more people. The objective of the World Bank or any other finance project is to bring benefits. And if the price of bringing those benefits includes paying a salary supplement to somebody, then I think it has to be done. If you don't, then those benefits which you are trying to move to hundreds, thousands, millions of people, just will not materialize when they need it most. Now, in regards to moonlighting, I think a private entrepreneur is perfectly entitled to pay somebody for moonlighting. If, as a result of moonlighting, the daytime work of the individual suffers because the lady or man falls asleep on the job or just doesn't work as quickly as they should, it is basically because they were not paid the right rate in the first place. So I don't have a lot of sympathy with employers whose staff has to go out and moonlight. Bribes? No, I can't sympathize with bribes. Not at all.

Establishing Accountability in Emerging Democracies: Public Service Ethos, Management Systems and Transparency

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Having been associated with the Consortium approaching 20 years, I find it very interesting looking back on the last 20 years and trying to project the priorities and orientation of international financial management for the next 20.

My activity in government was all borne of trying to make Bolivia a viable society. And that, basically, was the concept of introducing democracy. After leaving public service last year, I spent the last year at St. Anthony's College at the Latin American Center on a project, the viability of emerging democracies. Specifically, we did nine seminars on different aspects of the new Bolivian democracy. Basically, that's the area I'm headed in right now. I haven't forgotten the issues that concern me tremendously, especially during ten years in the Controller General's Office, where my task was to introduce the concept of accountability. But what has happened in this last year, especially, is that the viability of most of these emerging democracies is very dubious. They are highly vulnerable for a series of reasons, but I'm going to use only the Bolivian case.

To start, the premise of this presentation is essentially that public accountability is one of the fundamental requisites for the viability of a democracy. And it requires that those persons, elected by popular vote, or named, appointed by an authority, emanating from the electoral mandate, must respond to society as well as to policy decisions and their implementation. In a recent publication of the Consortium, an article on acountability states, Government accountability to the public has deep roots in representative democracies. That a government derives its just powers [its legitimacy, in other words] from the informed consent of the government is the very heart of the democratic system of government. I should like to also say that if accountability can be established, it can also serve in a very important way to reduce the abuse of power or the undue concentration of power. Accountability, transparency and oversight can be used as effective restraints to identify, to reduce, the opportunities for corruption, improve possibilities to identify it and develop the evidence needed to censure unacceptable behavior.

A gentleman who questioned Maurice Mould talked about the growth of corruption. I don't know whether corruption has grown or not. I've been fighting it for over a decade. What I do know is that it is much more public. Under authoritarian governments, there is no transparency. You can cover up. No one is held accountable. Perhaps that is one of the most positive things that has come out of these emerging democracies. Yes, scandals all over the place, but we're starting to look at it. I share Maurice's view that corruption will always be present. The problem is to control it get it under control. The best way to get it under control is by having a democracy that obligates people to bring forth these issues and denounce them.

Looking at democracy, accountability is thus inconsistent with the illegal nature of defacto authoritarian regimes. I can remember years and years when I've been brainwashed, as so many of us of my generation were, that democracy was not viable for us natives. We didn't have the education, we didn't have the content, and so on and so forth. I'd like to make the analogy that you can read a lot of books about sex, about making love, but the only way you learn how to make love is by doing it. And the only way we're going to learn about democracy and handle it, make it really productive, is by trying to live in a democracy, not just the formal institution, but in the elements that make a democracy viable.

Furthermore, accountability is certainly poorly understood. The concept is nonexistent in many societies. My experience indicates, and I can't say this is a rigorous research result, that accountability is a concept. And, as a term, it exists only in the languages of the countries of the societies that went to democracy via the route of the constitutional monarchy. It was, as the monarch's absolute power got limited, not just in terms of taxation. But when you had to account to a representative body on what you did with public resources, or why you took a society to war, you start to understand the concept of accountability. It is very interesting that in none of the romance languages, the Latin-based languages, does the term accountability exist. Check it. In Spanish, in French, in Portuguese, in Italian, it doesn't exist. I think it is interesting that none of these countries went to democracies via the route of constitutional monarchy initially.

Although Jim Wesberry has tried, for instance in Spanish, to use the term respondabilidad, I think the easiest thing is to just define it. I've been in Great Britain, for a second time, and they've got tremendous constraints on accountability. Have any of you looked at the Official Secrets Act of Great Britain? That is a total abuse of the concept of open government, of accountability. The United States only recently brought out this law on access to information. So, I have a certain reservation, and I am also concerned that, even in the developed societies, people are not really conscious of what is involved in accountability.

In Spanish, in my society, the concept of accountability conflicts directly with very fundamental traditions and values. We have the concept, principio de autoridad, the principle of authority. And it takes precedence over due process of law, over human rights. La majistad de estado, the majesty of the state, is the concept in a democracy of the state of service to its citizen. You have the autoridad publica. As Controller General, I was an autoridad. Someone seemed to forget the term, servidor publica, public servant. When they introduced it into the SAFCO law, there were tremendous protests. It was felt that we were humiliating public employees by defining them as public servants. So you see how difficult the concept of accountability is.

This presentation is about the Bolivian experience. I've had other experiences, but over the last 25 years, I have made a greater and greater commitment, as so many of my generation did, to Bolivia, to its democracy, to its institution. This has been a real experience, case study if you wish, and that's what we did at Oxford. I would also like to say that I enjoyed immensely, thanks to Jim and others, the opportunities to work on issues of accountability in Argentina, Paraguay, Peru and El Salvador. I guess the most moving experience was the one in South Africa where, a few months before the election, I was invited to participate in the sixth conference on the new constitution of South Africa, and the title of that conference was, Accountability, Transparency and Accessibility for the New South African Society. I also had the chance, at a conference of the World Bank in Jordan, to look at the issue of corruption in government, a World Bank project, but, you know, no one was willing to recognize us. We were wasting our time. It was an authoritarian government. A very decent one, but it wasn't a democracy. So there can't be accountability, not real accountability. There can't be real transparency. This is the problem when you start looking at these different alternatives.

In Bolivia, we finally went to democracy in 1982. It is interesting to analyze the dysfunctional government inherited by the new democracy. There were no systems. Forget about management information systems. Forget about management systems. Budgeting was the biggest joke I've ever seen. When I entered the Controller General's Office, we were supposed to be carrying the accounts of government, but there was no way to do it. I entered the Controller General's Office at the end of 1982, and I think the first accounts I brought out were 1977 or 1978. They weren't worth the paper they were printed on. At a meeting on this issue with at least 100 professional people, I said, The most important change we could make in the accounting report is not just accelerate it. We should publish it on paper that is absorbent, and use ink that is non-irritable to human skin, because that report might have some useful destiny for a society where there is such poverty and such a shortage of toilet paper.

The tragedy is we go through the motions. I saw the auditing system which we had in Bolivia. The auditing system was basically to do a review and find a noncompliance. And since there was such a hodgepodge, such an accumulation of regulations where each defacto government brought in new regulations, you could always find noncompliance. Noncompliance could then be carried to the criminal stage. At least they would be obligated to return the money.

To compensate for this breakdown in public administration, they instituted a system of pre-controls. The Controller General's Office was given the power and the duty to review and preauthorize any payment order, any contract, and so on. We had a tremendous accumulation of volume there. Of the 1,100-odd people in the Controller General's Office, something like 750 were dedicated to this pre-review and preauthorization function. What ultimately happened is, of course, we just blocked government and we became one of the most talented, capable, extraordinary institutions in the technique of extortion. A signature of one of the Controller General's officers was fundamental if you wanted to pay anything. I remember there was an import of a vaccine for measles. In a society like ours, which has a very high proportion of indigenous population that is highly vulnerable to measles, we blocked, for over a week, a shipment of vaccine to Bolivia because they couldn't fulfill the obligations. The man who brought the vaccine in didn't do it exactly according to the rules, and so the Controller, the guy who had to sign off on this and authorize its being brought in, refused. We lost a lot of children thanks to that delay of an additional week on the vaccine. So, it was a very tragic situation.

I think that democracies in this type of a society start off with a tremendous handicap. They inherited from the defacto, from the authoritarian government, total chaos and incompetence. And as far as public sector management, they inherit much less transparency and accountability.

We attempted to change in 1953, of course, when we went to democracy. We went with a hyperinflation process well underway that dated from the tremendous indebtedness that came from the mid-1970s. People seem to forget the payment flow and availability of petrol dollars, and so Bolivia got itself indebted under several military governments. It acquired greater and greater fiscal deficits and the military government kept instituting greater and greater controls. Also, because they could indebt themselves, and it was a period of rather good commodity prices, they undertook a series of public investments in industry and all kinds of activities. So, Bolivia ended up with literally several hundred enterprises that belonged to the State. This wasn't done by left-wing governments; this was done by military governments.

Maurice may say that there have been countries where public corporations, State corporations, were properly run. I think there is some background of this in France, England and Sweden. I remember a couple that I visited in my time. I would say that they were run in a mediocre manner. They weren't as bad as Bolivia, but then, you can't use Bolivia or much of Latin America as a standard. Nonetheless, we ended up in this type of a situation and ultimately, when we went to democracy, we were in the throes of an accelerating inflation.

The problem in Bolivia was: What's the priority? We already had inflation above 1,000 percent. If we want to bring inflation under control, then you had to bring in fiscal discipline. If you brought in fiscal discipline, then the country blows up. We had rioting in the streets. There were two amazing men in Bolivia's democratization. One was an old-time politician who came from the left who, when he was President, imposed a stabilization program in the mid-1950s. The other was an American Ambassador from Oklahoma. Between the two of them, they somehow were able to get the country to make the transition over to a democracy. The Ambassador would appear in military centers and took very strong positions. You knock off a left-winger, and forget about U.S. backing. For us, in Latin America, it was amazing. It was the first time that I could think of, in our history, where there was a determined effort to back a process of democratization. Between the two of them, they made the bridge. The left-winger committed political suicide, because the inflation really did get out of control. He didn't try to bring it under control, and we ended up with a 24,000 percent annualized inflation rate. He had to cut short his term by one year. But, we did make the transition to democracy, and then we made the move to getting the country stabilized.

I would like to also point out that Bolivia has been held out as one of the really exemplary cases of putting order in their economic house. With the democratic government, where you had to respect people's rights to protest and so on, we were able to stabilize the economy. Over the period from 1985 to the 1990s, we were able to bring down the hyperinflation very quickly to something in the 6-10 percent range from the 24,000 percent level. The World Bank and the Fund, of course, use this as the great case or the great success story. That makes me very nervous because, looking back over my life, I remember when the World Bank and the Fund used to bring up Pakistan as the great success story. What a tragedy. Remember when Columbia was the great success story? So, the moment you get the blessing of the World Bank and the Fund, many of us become superstitious. We think that's the kiss of death. I'm worried about it and I think we're starting to have real problems because we are held up as an example.

Of course, neither the World Bank nor the Fund really made an effort until at least a year and a half after we brought in stabilization. They had missions and so on, but they never really disbursed one cent. The stabilization in Bolivia was done at the cost of introducing tremendous poverty and underemployment. The international agencies did not respond until a year and a half after. It was so difficult that I remember there was a meeting to discuss this after stabilization and Bolivia had hired Jeff Sachs to be one of our advisors. The IMF said, No, he cannot participate in the meetings. But he is our advisor. They refused to have the meeting unless we eliminated Jeff Sachs. It was that bad. I'm not saying that Bolivia didn't have some good economists, but certainly Jeff had some very independent points of view and he wouldn't run away from these institutions. So, I do fear for Bolivia because we are being held up by the World Bank and by the Fund as the great example of success and structural adjustments in democracy.

Unhappily, and we might as well face it, stabilization and economic order are fundamental for any country. But let's not kid ourselves. It does not bring any real benefit for the great majority of the population. To the contrary, you may have order and discipline, but what happens is you polarize the society even more. In Bolivia today, at least 70 percent of the population lives in poverty or extreme poverty. They do not participate in the benefits of this stabilization, which has brought a modest growth rate of 3-4 percent. This only benefits a small part of the population. So, this exclusion is a very serious component of this society which is trying to establish democracy.

I have come to three conclusions. I call them the components or conditions to establish accountability. I grouped them in three, and I'm going to take them in inverse order of the title of the talk. When I developed the talk, I found there is a sequence in which one depends on the other.

The first, for accountability, is transparency of government operations. I think that is the ultimate condition for accountability. It is not merely publicity and accessibility to government operations information. Let me be more specific. First, if there is going to be real transparency, there's got to be a consultitative policy formulation procedure. This means public meetings. It means publishing policy proposals and giving people the opportunity to question them and have public hearings on them. This is not part of the Latin tradition. It is not part of the tradition anywhere except in certain countries at a national level. It is more an issue at a local or regional level. I think this consultitative policy formulation is very important. You don't have to agree with what people say. Some people have an axe to grind. But, more and more of our policies would be much more effective if this consultitative, open process existed.

The second requirement is an accessible system of relevant, reliable and timely information, comprehensibly summarized and publicized. It is not enough to have a good information system and that it be accessible. There must be a process of summary and explanation which makes it comprehensible to a great portion of society, at least that part of society that has a minimum level of education.

Third, there has to be an independent and qualified post evaluation of policy implementation, verification of its results, and an evaluation of management and information systems (how effective and how efficient they are), particularly the internal controls. There has to be an evaluation of results. That's the name of the game. It's not compliance. It's not financial statements or auditing that is most important. The first thing to evaluate should be audits of management and information systems and their internal controls, to see how they're functioning. The second one should be performance auditing. The third one, and I know there might be some lawyers here, would be compliance auditing.

The fourth thing I look for is responsible and opportune oversight functions fulfilled by Congress and other representative bodies. It is inconceivable that in congressional institutions, any representative institution can exercise the oversight function even if it doesn't have a very well qualified and independent source of opinion as to what really went on, or what were the real results. This is typical in Latin America. In Bolivia, which isn't typical, the Office of the Controller General does not report to Congress. It reports to the President, although Congress, under the new law, gets a copy of everything we do.

The fifth thing, and this has become very important to us in a society that has this very vertical socioeconomic structuring, is devolution toward local government of those public services and investments that most directly affect people. At the local government level, organizations have a say in determining the allocation of limited resources and also in performance auditing, especially for those services such as education, health, local roads, micro-irrigation projects, and other services which directly affect people.

Finally, and this is perhaps one of the most difficult things to acquire in our society, a well-developed investigative and prosecutorial capability which respects due process, civil and human rights, as part of an independent, qualifying, expeditious, accessible, and trusted judicial system. It's got to be based on fundamental legal principles. It is not just the rule of law that is involved, it is the administration of justice and the application of the law. Many of the laws in our societies, because of the many years of defacto governments and so on, are really barbaric. Let us not forget that there was a very strict rule of law in the Germany of the 1930s and early 1940s. The law was terrible. Are we forgetting that there was a very strict rule of law and a great legal tradition in Chile during the whole Pinochet period? So, let's be careful. We call it legal security to differentiate it from rule of law. But the most difficult thing is investigation, and when criminal investigation is in the hands of the police force, you can get yourself into real problems.

I really think we should have an independent investigative unit which handles, in specialized units, the investigation of different types of possible crime. Not just common crime, there should be a unit on administrative and financial investigation and so on. In a county like ours, probably the most important unit we're missing is one that investigates the abuse of human rights, especially violence to women and to children. You call it domestic violence. It is much more profound than that when you have a society with the type of structure we have. We must have the capability to investigate and we must have the capability to punish. One of my great failures, and I have a good list of them, was we tried to bring forth a law on violence to women and children. We maintained that these crimes, beginning with rape, beating up, and so on, are still private crimes. They are not public. It is not obligatory for public authorities to prosecute them. I lost that one by one vote. I was the only vote. But at any rate, we move ahead in the society.

So that group of components are what I call the tools that permit us to have a reasonable degree of transparency in public operations. But, to be able to exercise these tools, we must also have public resource management systems, my second conclusion. Otherwise, there is no way that any of these tools can be applied. They begin directly with the whole issue of programming, implementation and public policy, programs and projects. We call it operating targets and sequence and inputs programming. Organization and support services are required to execute that operating program. And, of course, there are financial requirements. We are still doing budgeting in Bolivia. We pay lip service to operating programs. But it is an attempt. We are beginning perhaps.

Basic to public resource management is the management of public personnel. Personnel development and management is the saddest part of all. We are introducing, thanks to the assistance of the World Bank and their consultants, a system of civil service, whereby there is absolute rigidity. If you can get a job, you can't be kicked out of it unless you can be tried for malfeasance of some type. There is no sense of a civil service system which continually guarantees the upgrading of the civil servant. So, in other words, by putting in these rigid restrictions, what we're going to end up with is mediocrity. The level from which we are beginning is unacceptable. I can get into a long discussion on this issue, that we need a good civil service, but you may not like it. For a society with a high degree of poverty, and with a need for a good public sector, the real solution is a system of promote or out. The promotion has to be objective, but you cannot continue to have a system where you just maintain an employee forever. Unless he does something really barbaric, he's not allowed to be taken out of the public service. In the long run, the people we serve lose.

Then there is the whole problem of supply of goods and services and, of course, the management not just of the cash flow, but of the debt. We have not had good success in that area.

Based on these things, we need a good management information system. I was surprised to hear Maurice say that accounting will go out the window. I believe that management information systems have to have performance criteria, otherwise they don't have very much to do. But I haven't found yet, and I'm not an accountant, anything that substitutes for building a management information system. At its base has to be good financial statements and internal controls. So, if you want to apply the tools of transparency, you'd better have good public management systems.

Finally, the real quid, public service ethos. I mentioned the problem of the concept of public service early on. If you want management systems to be purely nominal, they work when people are committed to them. And people are committed to them when they have a sense of public service. A commitment to public service with accountability, in contrast to the rights of a public authority which often is used to justify impunity, is fundamental. For this we need clear principles and guidelines as to expectations, responsibilities, acceptable and unacceptable behavior. It is a values issue. Do we have the capability to face up to values issues? Issues such as conflict of interest? Here we have an administrative law of procedure whereby your accuser, to whom you owe tax money, is the man who at the same time is your judge. He accuses you and you have to defend yourself before your accuser. That is a violation of due process. That is a violation of your right to defense. And yet this permeates administrative law, but not just in Latin America. It is all over the place, including the United States.

We need continuing civic education on democracy, accountability of public service, at each level of schooling, and especially in basic social organizations such as political parties. Wouldn't it be wonderful, then, if you want to be a member of a political party, you have to take a test? Remember when there was a test to become a U.S. citizen which tested whether you knew your constitution or not? Political parties are not ever held accountable. Maurice is very right. They are a private organization. How about these big public service organizations? These NGOs? Are they ever accountable? I'm very worried about them, because there is not that ethic of responsibility to society.

Finally, we need incisive, opportune and competent reporting by the media on government policy, its operations, results obtained and integrity. That's part of democracy. If we keep stimulating this, we're going to have more scandals. We're going to have more corruption become public. But, is it because there is more corruption or because we're making it public?

Let me end. What have been the advances of the last 30 years and the requirements for the next 20? The conclusions of the Oxford Research Seminars on the Viability of Democracy in Bolivia showed, first, that there is a growing scope and intensity of poverty in Bolivia. There is a deterioration of the rural sector and exclusion from human development services, education, nutrition, sanitation of the great mass of our population, because we've got to keep our budgets. This means that more than 70 percent of the population of Bolivia have no stake in democracy. I think it implies that we will have violent confrontation in the not-too-distant future, especially as this situation intensifies as a world economic and financial crisis.

Also, there is a continuing reduction of participation in the political process, because people don't have a stake in the process. We're concentrating power. Political parties are contracting their membership to the group that it really benefits. Of course, there is campaign financing. Frankly, the effect of this on the representative institutions of this Congress is shameful. I talk about Bolivia. I'm talking about a country that just started democracy 16 years ago. But it is still a fundamental issue.

Finally, the third group of problems relate to the insignificant advance in establishing accountability, transparency and legal security. Those three fundamental institutions for democracy take a long, long time. They take a fundamental change in attitude. If we don't have it, we have serious problems.

Let's take a look at the SAFCO project. We had no success, or such an insignificant success that it's called a zero, in establishing the public service ethos, and in upgrading the civil service. We have had some success in auditing and in budgeting, although it is still rather arbitrary because the operations program meaning is not only misunderstood, it is only operating nominally. Auditing has reverted to the mechanical identification of noncompliance with one or another regulation. Again, it is easy to find noncompliance because we have so many regulations. For every regulation that says X, I can find one that says Y that contradicts it, because we haven't cleaned up that mess. Performance auditing is nil. I've come to the conclusion that training and post-graduate study cannot compensate for the basic deficiency of professional formation. We try.

So, you give me the paternity for the SAFCO project. Let's have the honesty to recognize the limits. How far did we go? Very little. And yet, I do not give up. I believe we have to continue. With essential components for future development of accountability first, we have to go after this public service ethos this fundamental change in attitude. And we have to promote a reallocation of public resources to those issues that can provide a viable society. How are we going to overcome this extreme poverty? How are we going to integrate society where a much greater percentage of the population has a stake in maintaining a democratic system?

You discussed this with Maurice. I think we need a reformulation of curriculum and a standard for a degree in management systems. I think we have to stop having degrees in accounting and auditing. Forgive me. I think accounting and auditing is part of a much greater thing, and it is not just financial management. It is public resource management. It is the whole issue of orienting it to people who perform. And one thing in my lifetime that I've always been fascinated with is economic condition in Latin America.

Everybody dedicates themselves to giving courses on how to prepare and analyze project feasibility. How do you prepare projects and analyze their feasibility? Very few people give you courses on project management. I can tell you I'm one of the experts on project preparation, and I can make almost any project feasible or unfeasible. You tell me what you want and I'll do it for you, because I have a good feel for the issue of sensitivity analysis. So I look at it at the university level, and at the on-the-job-training afterwards. There has got to be this beautiful apprenticeship. In the old days you went to some type of an accounting firm for five years if you didn't have a university education, two years if you did. Then you had a public examination. I do not think universities should give the public examination. I don't think the qualification can come from the university. They may prepare you for it, but if people can't pass a public examination, it means the university is not fulfilling its role. So I would like to promote the reformulation of the curriculum and a standard for a degree in management systems which includes, but is not restricted to, accounting and auditing.

Based on these fundamentals, public service ethos and a basic training in the area, we do have possibilities to develop management systems on the tools of transparency, and thus the possibility for accountability. Without this, I don't see much possibility for accountability. I see even less possibility to really control corruption, and, regrettably, at this stage of my life, with nine grandchildren and probably several more on the way, I am most concerned with the viability of the democracies in my world. Thank you.

MR. HAMILTON (United States): The analogy you made between the emergence of democracy and the evolving of accountability in the constitutional monarchies was very interesting. During your brother's administration, I know there was a great movement toward fiscal decentralization. As you were talking about the poverty and the 70 percent of the indigenous population, what impact does fiscal decentralization have on this? I hear a lot about Bolivia being used as a model on fiscal decentralization. Do you see that process continuing, and do you see it as a tool for bringing decision-making down to the core of the population, and further democratizing the society? Just as a footnote, I know that when you were making your first fights for accountability, you were struggling against an authoritarian regime. That regime is now in a constitutional mode. Will this process continue?

MR. LOZADA: That's even more loaded than my speech. Let's start off with the thing of decentralization. Don't forget the devolution to local government was only about the middle of a four-year term, and there was only about two years of effective implementation. In the 311 municipalities in the whole country who converted municipalities into territorial municipalities, I don't think there were more than about 50 that really were able to benefit, that really used this opportunity. It was too short a time. And, obviously, with this we transferred a lot of resources to local governments. The people who most benefitted from it were the really rural communities. The big, urban centers did not really incorporate the population into this decision-making and oversight function. I think it is a process that is going to take a generation or more to really be successful. But I'm not willing to give up on it. However, I must be realistic.

This meant a decentralization of economic and political power from the capitals of the departments, where we have groups that concentrate economic, social and thus political power. There has been a reversion, so much so that until the middle of this year, only 20-some percent of the budget for the departments, for instance, had been disbursed. However, they're going to stop it, because this really affects the existing power structure, and they're not going to accept the existing power structure. And what they're not willing to recognize, and this is our great problem, is the greater your power, whether it is economic, political, educational or cultural, the greater your responsibility is to the society to which you belong. That has not been a principle that has gone very far in Bolivia. We have an excellent representative of the IMF who is backing this. They're using the pretext of indebtedness and things like that. The present riser-up in Bolivia is a man who was there during the former dictatorship and has been asked to return. I don't think the Fund could have made a worse decision, because he's totally whitewashing the present government.

So you can criticize a lot of the decentralization, and I think there were major errors, but those errors could have been corrected. One of them was that we divided education decision-making. Certain decisions were made at the central government level, and other decisions such as salary payments were made at the departmental level. But the running of the schools was at the local level. So who is responsible?

My brother's forte was not management systems. But he's a great guy for trying to make a viable society. I think it needed much more time, at least another 10 years, before it could really function. There had to be a lot of adjustments. What was your other question?

MR. HAMILTON (United States): I think you covered it very well. But there was one other aspect, and that is, I think, the regime of your brother was very big on the social issues which you mentioned.

MR. LOZADA: Well, as a man trained in philosophy, he feels that to make Bolivia viable you have to incorporate a great hunk of society into the decision-making process, the political process, and thus give them a chance to benefit from the economic process.

MR. DECENA-LUGO (Dominican Republic):You pointed out that in Bolivia there was a specific organization for controlling financial aspects, if I heard you correctly. Whom do you think should supervise the economic administration? Should any citizen have the initiative of being able to check, or should there be an organization? Should it be Congress? Who should have that initiative in your opinion? Also, I see that in your presentation it says that you are an ex-Senator from Bolivia. Also, you are the Comptroller of your Ministry of Finance. Why didn't you talk in your native tongue?

MR. LOZADA: Very well said. Let's comment about the last question. I understand that they are making a recording in order to publish this in English and they're not recording this in Spanish. In order to facilitate things, I spoke in English. I have given it in Spanish and I've given it in English.

Accountability is the duty of responding to the efficiency of public administration. And there is a single word in Spanish that will allow us to do that. But who is going to supervise it? Well, in a democracy, a representative body has to do the supervising, and any citizen can do that supervising. The problem is how to ensure that this supervising job is done in a responsible manner, based on information generated by people who are qualified. Let me reformulate that. I think that the function of supervising by Congress would be much more adequate if the Controller's Office of the nation had answered to the Congress, and specifically, to a bicameral commission of the two permanent chambers of the government of the public accountant. Where there were representatives of all parties of the government, obviously, the impartiality of the Controller is retained. However, I feel it is very difficult to do this because we have confused the Comptroller with the concept of Auditor. It is more legitimate to call him an auditor because the auditor generates an opinion, not a truth. An auditing report is not a truth, it is an independent opinion and a qualified opinion. Based on this, the real accountant or the Senator or the Deputy of the Chambers or an advisor or the Member of the Municipal Counsel or whomever will have to carry out his supervising. It is essentially politic. But this political thing could be a disaster if we didn't have an independent opinion, a qualified opinion. In the case of Bolivia, we created a committee, a vigilance committee.

MR. DURNIL (United States): Thank you very much, Antonio. Having visited Bolivia several times myself, there is one thing you remember. The airport there is at 14,000 feet, so it's very high up in the air. Another thing, I happened to be there when they had a devaluation of the currency. You were talking about the 24,000 percent inflation. On Monday, they eliminated three zeros off their bills of currency. So the Boliviano that I had worth a thousand was now only worth one. It was hard to figure out the exchange rate on that. Thank you very much for coming, and I enjoyed your presentation.

Status of Integrated Financial Management Systems in Latin America

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Today, I would like to explain first some of the basic concepts and assumptions of what we refer to as Integrated Financial Management (IFM) systems. Then I would like to share with you what I consider to be some critical success factors for these types of projects. Finally, I will speak briefly on the situation of ongoing IFM projects in Bolivia, Guatemala and Nicaragua.

Going to the basics of IFMs, what I want to highlight is that there is a group of core systems that start with the budget at the beginning of the fiscal year. These systems are used for budget preparation and then, during the fiscal year, the actual expenditures are compared with the budget. This gives us the budget execution situation, and the same transactions are used to keep track of the government's accounting. With that information, the government is able to manage its cash flow. Essentially, these are the core subsystems. There are other systems that can be implemented, such as human resources, fixed assets, procurement, inventory and the national debt (both domestic and external sources). On the revenue side, there are internal taxes and external taxes or customs.

I mentioned that there are some common systems used in several countries that were developed by the UNCTAD. The basic principle in all these projects is that there is centralized normalization whereby all the methods, procedures, software, training programs and hardware are defined once, at the center. Then these things are replicated in different locations. In each of the locations, which are called decentralized locations, there are the replicated systems and local staff is responsible for operating them. I mention this because there are some countries that are only now starting with these type of projects such as the Dominican Republic. It's interesting that they hear this, I think.

So, from a computer point of view, what we have is a number of units where the data are entered locally and then the data starts flowing up in the hierarchy. Some of these units may be part of a ministry, and some of these may be independent and report straight to the Ministry of Finance.

Essentially, at a point in time, all the information is consolidated at the Ministry of Finance, and then it can be accessed for queries and analysis by the central bank, by the President's office, the Auditor General of the country, the Congress and the community, if appropriate. Revenue agencies also receive and provide information on the tax collections.

Based upon the experience of these last few years in IFM systems, we think that the operational decentralization is appropriate, because if the data is entered at the source, where the transaction actually occurs, the possibility of errors is diminished. Secondly, if data are entered as soon as they happen, delays are lessened and the government therefore has a clearer picture of the financial situation. It is faster and more up to date. Finally, decentralization creates a sense of ownership and accountability, and transparency is enhanced as well.

Earlier this year, in May, there was a workshop in Peru sponsored by the Peruvian Controller. At that workshop, many IFM system users from different countries spent several days discussing the critical success factors for these systems. Why do certain projects succeed and others do not? We were able to identify several categories which I will develop now in a little more detail.

The single, most important success factor is to have high level support within the government. I think, in today's presentation, Mr. Arévalo from Guatemala made this point very clearly. He said, Look, unless there is a clear will from the government to push the system, it won't fly. It won't fly because there is a lot of resistance. First, because people don't like change, and, secondly, because of shifts in power. As an example, in an old system, many people have the power to approve or not to approve a supplier's invoice, and can decide whether that supplier is paid earlier, on time or later. When a new system is implemented, the system itself defines the payment date. So the person who had that power in the former system will lose it, and will resist implementation.

In addition, there will be a need to create a legal framework for the system to be implemented. That means a lot of political battles have to be won in the Congress to get these laws approved. All of this points to the need for the highest level of support. Ideally, this should be the President. If not the President, maybe the Vice President, or at least a Minister. If that support does not exist, it is not worth starting because it won't fly. It won't work. Once the system is in place, the government starts turning around the system. The government cannot function without the system. So, that is something that the government has to realize.

There is also a need for clear assignment of responsibilities. This is true of every computer-based development project. You need to have a clear leader who is dynamic. Many of you are aware of projects that stopped when the director left. I know of at least two in Latin America where the project director moved to another position and the project was over. The personality of the project director and the people managing the project is very important.

There has to be a balance between the people who know the financial aspects of the program and those who know information technology. It is obvious that these types of systems cannot be implemented manually, and that they require the use of computer tools. But there has to be an equilibrium between the experts on information technology and the experts on accounting and finance participating in the implementation.

There must be teamwork. Team members include management or top-level government officers. The team can also include donor institutions like the IDB or the World Bank that participate as well, along with information technology experts, auditors and end users. Everybody has to be a part of the team, and no one should be left out.

There has to be a good plan. The plan has to be kept up to date, and everyone must be informed of what the plan is and how we are executing the plan.

The end user participation is especially important. One of the things we have seen is that people tend to reject solutions that are forced upon them. End users need to participate so that they feel that the system is a solution to their problems, and not like something that comes out of the sky. After all, it is the end users that will have to enter the data, and that data has to be entered accurately for the system to work properly. We have to find incentives for these people to enter the data on time and without errors. One of the ways to ensure this is by allowing them to participate in the development of the system. For that purpose, one of the things that can be done is to create an end-users group that has an advisory role or a participative role in the development of the system from the beginning of the project.

Regarding the computer-based systems, one interesting question is: What do we mean by integrated? What is integrated? From a systems point of view, the system is integrated if it uses just one single database, but it has to be developed as such from the very beginning. I know of a certain project, and members of that project are here in the room so I won't say which it is, where they said, Okay, let's develop a system for budgeting. Let's develop another system for accounting, and another system for cash management, and because we are going to use the same database language, it will be easy to exchange data between them. That will make it integrated. Well, that is not true. That is not the way to make it integrated. The way to make it integrated is to consider that all those data are part of one single database. Certain end users will utilize the database to enter cost information, others to prepare the budget, or to do the cash management. That is one single database, and everyone is looking at the same database but from different points of view.

If at all possible, it is better to use an existing system. Why? Because development of the system is always an unknown. You only know when you start, but you never know when you're going to finish, and you never know what the end product is going to be. Maybe it will be a great system, and maybe it won't. If there is a system you can see, you can touch and you can see in a demonstration, it may not be the perfect system, but at least you know what you are getting. You know that with certain changes or modifications in a certain reasonable amount of time you will have a system. When you start from zero, you never know what you're going to get or when you are going to get it.

There are security issues that need to be addressed because hackers or unauthorized people who get into databases exist in all countries. These things have to be addressed at the time the system is developed so that data integrity can be ensured.

It is better to start with a system for the decentralized locations rather than with a system for the Ministry of Finance. Surprisingly enough, this was a conclusion in Peru. Usually one would have the feeling that, Well, let's develop first the system for the Ministry of Finance, and then we go to the periphery. According to the experience of the people attending the workshop, it is better to start with the system for the decentralized locations. The reason is the following: At the decentralized locations, they need to keep track of all the transactions, the cost information at the lowest level of detail. They need to know their vendor. They need to know the invoice number. They need to know when the purchase order was issued. They need to know all the details. As information flows up for consolidation at the Ministry of Finance, the information is being summarized. For instance, the

Minister of Finance does not care what the purchase order number is. All the Minister wants to know is how much money a certain ministry has spent in gasoline, or in vehicles, or whatever. The Minister doesn't care about each purchase order. So, if you have a system that works at the full level of detail, that same system can help you get the consolidated information because it's much easier. You just summarize.

Finally, you should take special care with the output reports because that is what many end users get to see. They don't know what the database looks like. They don't care. It is something that might be beyond their understanding and their interest. What they see is what they have on the screen or the printout they might get. That is especially true for the higher managers that will be receiving this information such as ministers or even the President or the Congress.

Now, as you decentralize, you lose control. When all the information is being entered at the Ministry of Finance, you have a good level of control there. It is just one single place where people are entering data. But, as the data entry operation and all the transactions happen at the decentralized locations, you lose control. So the only way you can keep some control is by increasing your audit capabilities. That's why, in Guatemala, they have created in each decentralized institution, a unit that takes care of information technology (in the sense of data entry and data processing) and also they created at each of those institutions, a subsidiary, let's call it, of the Controller's Office. So, they need to have those two new units in each of those decentralized locations to keep everything under control. For the same reason, the Controller's Office must participate in systems design, because who knows better than the auditors which controls must be built into the system. If a system has built-in edits and controls, errors are avoided at the very beginning, as soon as the data are being entered, and very few errors will flow into the database. So the wise thing to do is to get auditors who have some knowledge of information technology in general and a good level of knowledge on the IFM system in particular. Otherwise, how will they be able to conduct their audits unless they know the IFM system, since all the accounting transactions of the government will be in that system?

Eventually the development work is over and the system starts being used in a production mode. How do you ensure that this is sustained? One of the things that happens, the end users keep rotating. There is a lot of turnover in the government so you will need to maintain a permanent end-user training program to keep training people as old employees leave the government and new employees are hired.

The complexity of the whole operation will increase. It will not become simpler, but rather more and more complex, in the sense that while you keep the system restricted to the capital city, everything is more or less under control. But as you start decentralizing and computers are installed in other cities outside the capital, the complexity of keeping all these installations running increases. It gets tricky. You need to have maintenance service to fix the computers in cities where those government installations might be the only ones that exist. But you will still have to find a way to keep those computers running.

One of the problems I have seen in many countries is the problem of salaries, in the sense that the government salaries are lower than those that are paid in the private sector. Very frequently government employees are trained and, soon after being trained, they leave and go to work in the private sector. One of the solutions for that, as another speaker said this morning, is to increase the salaries. But if that is not possible, one of the alternatives is to out-source the operation of the computerized system from the very beginning. I mean, if you implement the system in-house and later on you want to out-source, it is much more complicated because all the people who are working in-house running the system will lose their jobs. However, if from the very beginning it is out-sourced, then nobody loses their jobs because nobody was doing the work from the very beginning.

Another thing that happens is that hardware and software have a very short life. Yesterday we had the 286s, then we had the 386s and the 486s, now the Pentiums, and so it goes. It keeps changing. Every couple of years there is a new thing. Sometimes you can keep on working with the old technology, and sometimes the changes are such that you need to move on and get the most recent technologies. You will need to plan for all this.

There will always be a need to modify the system, and that is what we refer to as systems maintenance. Here, the most important question is, What programming language was used to develop the system? Depending on the answer, it will be either easy or difficult to make the changes. Secondly, sometimes systems use parameters, and just by changing those little parameters, the system will behave differently. But if that methodology was not used from the very beginning, then you cannot do that, and it is more complicated to make the changes.

Another thing that can help improve the results of implementing one of these IFM systems is the government use of electronic transfers to make payments in lieu of issuing checks. This works much better than checks. It is faster, more reliable, and there are less possibilities of fraud.

Another thing that helps a lot is to have one single government bank account. Otherwise, there is the problem of the government having money in many accounts and not knowing where the funds are or how much money is in those accounts. Then the government may go out and borrow money and pay interest while money is sitting in different bank accounts doing nothing.

Of course, the communications infrastructure in the country has a lot to do with decentralization. It is very hard to decentralize if you do not have good communications, and you cannot transmit the data from the decentralized locations to the central location at the Ministry of Finance for consolidation. So, a good communications infrastructure will have a lot of influence on the success of the IFM system. If the communications infrastructure is good, then you will also be able to implement electronic mail, and you will even be able to create an Intranet.

That is all with regard to my introduction. Now I will refer to the first of the three projects I was asked to discuss. When I refer to these countries, Bolivia, Guatemala and Nicaragua, I am referring only to information technology, to the computer-based system. I am not talking about other philosophical or legal issues related to this subject.

Bolivia started in the 1980s with this IFM idea, and at that time, philosophically, Bolivia was far more advanced than the rest of Latin America. Unfortunately, I have to report that today they are far behind most of the other Latin American countries. They have only decentralized the operation of the system to five or six states. Otherwise, all the data entry operation is performed at the Ministry of Finance in La Paz. So, although there are another 10, 12 or 15 ministries, these ministries type all the information of each expenditure and send a paper document to the Ministry of Finance, where the same information is typed again. This has generated considerable delays. Sometimes the document may have one little mistake so it is sent back to the original ministry for correction, and then returned to the Ministry of Finance. It is really not very efficient.

Their system works in what is called character mode, as opposed to graphic mode. Graphic mode is Windows. This is a very old system that does not run under Windows. The hardware is in terrible state. There are machines that are 15 years old or older, and they are still being used. At this point, it is likely that these machines cannot be properly maintained. If they break down, there are probably no spare parts to fix them, so it is a very critical situation. I was there earlier this year, and I was really disappointed.

Regarding Guatemala, you have already heard about this project from the first speaker today. This project is going really well. From my perspective, the project started in September of 1996, because that was when the World Bank loan was approved. The system was implemented on January 1 this year. It was developed by a Mexican consulting firm. It is being used in a decentralized manner by more than 30 ministries and other agencies. The 1999 national budget was prepared using the system, and has already been submitted to Congress. A second loan from the World Bank has already been approved for the implementation of many of the subsystems that I mentioned were outside the core systems. They have their own Web page, and you can go there for more information.

Finally, the last project I will report on is Nicaragua. The project started back in 1995. They visited several countries, including Bolivia and Argentina, and they finally decided that the system that better fulfilled their needs was the Argentinian system. The government of Argentina donated the system. So, they are using the Argentinian system after modifying it substantially to adapt it to their own needs. They also started in January of 1998 in theory. In practice, they started in February and March, and they had to load the old data that existed from January 1 before they were able to start entering the daily data. They caught up, more or less, in April and May. I understand that they have, as of the end of July, a clear situation of the government finances. They had an old batch system running on an IBM mainframe that has been discontinued. They threw it away and they are completely relying on the new PC-based system. They are now working on a new software package for data entry at the decentralized locations, because at this time data is being entered centrally, but that's is just because the software is not appropriate for decentralization yet. Since the system was developed in Argentina many years ago, and my colleague here will talk more about it, this is not a state-of-the-art system. Its life span will probably not be very long, but it will help Nicaragua gain experience and will give them a start in working with computers. Then the transition to a new, more modern system will be easier.

Thank you very much.

Jim Wesberry, Casals and Associates
Director, Americas' Accountability/Anti-Corruption Project

Consistent with the theme of our conference, The Past 20 and the Next 20 Years of Governmental Financial Management, I'm going to make a few announcements before we hear from the next speaker.

In this room, today, we have two very distinguished people in government financial management who are quite historical. Toward the back of the room is Dr. Ray Einhorn, who is the Vice President of the International Consortium, and runs our forum. He was a member of the team that developed the original accounting principles and standards for the United States Government in the 1950s, which later became the model system, the framework, for United States governmental accounting. He has been a leader in the accountancy profession lo this many years.

Up here in the front row is Dr. Mortimer Dittenhofer, father of the Yellow Book, the GAO standards developed as the result of a project that he directed for GAO in 1971. Both of these very distinguished men hold a place of honor in the accountancy profession. They played a major role in bringing governmental financial management to where it is today.

Now, Alberto Arolfo will talk to us about Argentina.

Alberto Arolfo, Former Accountant General of Argentina

Up until last month I was a direct participant in the reform of financial administration within the Argentine government. I recently left my position as Accountant General, but I'd like to share some of my experiences with you.

We started the process of reforming financial administration within the government in 1992. We had the following objectives: to carry out management of public resources in a framework of complete transparency, to ensure that public administration is done economically, efficiently and with effectiveness, and to generate a process of information that is timely in order to facilitate decision-making.

One of the most important aspects of this project was the integration of all of the financial administration systems' internal and external controls to ensure optimum efficiency. This is the fundamental point to which I'll be referring because, specifically, integration of the system from the technical point of view requires greater attention on our part. From this point of view, we have to establish certain indispensable requirements to guarantee integration of the system.

We started out with the principle that there would be one single budget and it would be applied universally. It would cover all of the public institutions and would not be a collateral budget. To ensure complete integration of the system, we established a universal concept for income through all transactions that produce a source of funds. This means that we have common terminology and language, and the same concept existing in the budget as well as in the accounting. It was essential to standardize these two components to get a consistent and reliable flow of information from the system.

In the same manner, it was necessary to establish the concept of income. What do we mean by income? It was also necessary to establish a good concept of what we meant by expenses. For income, we counted all the common incomes coming from taxes, the ones coming from administration functions, etc. We counted, as well, all diminution in the assets we might be joining together. Any reduction in the assets produces an effect in the income of funds, just as the liability also brings an increase in the debt as a transaction. Against that we have the usual expenses, the increases of the assets and the nation's diminution of our liabilities which indicated to us the concept of expense itself.

Once we established all these in our minds, it was necessary then to determine how we could carry this integration. What is the appropriate moment to capture this information? And how do we establish a direct relationship between different classifications in the budget and in accounting? That is why it was necessary to establish different points in time in carrying out the budget. Once we defined these points in time in the budget execution, we found the moment in which the plans integrated with the different budget concepts. So this was the moment where we defined the subject, and this was the appropriate moment to capture the information.

In building this system, we found that many different organizations would be providing information to this system. There are different organizations from the Budget Office, the Office of Tax Collection, Customers, etc. All of these are entities in the central organization. And, of course, there are the entities from the decentralized organization, the Treasury. All these institutions would be collecting information and inputting that information through different databases and through related databases. It all got connected in the database of the financial system and gave us the results of the different outflows of information, information that was directly related to the needs of the financial analysis. Here we have the different outflows of information to carry out this project our expenses, our different classifications of the type of expense, plus the economic classification of the institution. The accounting system, as you know, balances all the different uses of funds that we in Argentina would call the financing and savings schematics. It has the capability to relate the different incomes with expenses associated with an economic classification. All of this is related to the national accounting system, or economic accounts within the nation, and also to statistics for public finance which is a reference of framework which ensures that all of these mechanisms are functioning within the system.

Even though we had defined the how, when and where, the information was going to be produced, we needed to determine who would produce the information. It was necessary to better define the different accounting entities, since our final objective was to find integration, direct integration, between the budget and the accounting aspect. From the point of view of accounting, we defined the accounting entity as the different accounting organizations that form the central administration of the country integrated by legislative follow-up, both judicial and executive, the different ministries and their different dependancies. All of these together constituted an accounting entity. Also, each one of the components constituted in itself an accounting entity. There were times when we found similarities or the same language used in the processing of transactions among the organizations in the accounting entity. We also found definitions in the accounting entities in the operation of their systems that were based on a single data entry satisfying their needs for information. Our task, to integrate the systems, was a lot easier to do, and quicker when we were able to find this type of relationship.

In the first place, we had the structure of our budget. This is a structure that is predicated on economic classification. Therefore, we can call it a universal structure, if you will. We had the structure of our budget and the structure of the accounting plan for accountability. From the point of view of the budget, we have, first of all, a checking account, if you will. In this we analyze and compare expenses with incomes. The result of that analysis is an economic classification known as savings. Now, a capital account, which involves all of the public investments is all of the expenses in the capital against the different resources that we have in our capital. The checking account as well as the capital account determine how the State defines its own financial operation. All of the expenses can be reviewed to determine how payees meet their objectives and how they carry out services. This is what makes up what we normally know as the collection of decisions to be made in the formulation of a budget.

We have two big groups of accounts, basically. Some accounts are accrual. The other accounts inform us about the results of a particular year. Well, then, everything that has to do with the current accounts as to its structure is precisely that which informs us about the results of the accounting. Everything has to do with the various expenditures of capital as a consequence of the execution of the fiscal budget. This impacts the detrimonial accounts as a debit as incorporation of fixed assets and assets are produced which are registered by accounting. In the same way, everything has to do with financing. This is the part of the group of decisions that the government makes, which also makes up a part of the policy of liquidity. Each one of the applications that in turn constitutes debits are reflected by accounting, which records them. This, in itself, is the heart of the entire matter of integration. In order to achieve precisely this integration, it has been necessary to establish all of the criteria from the point of view of budget as well as accounting. These are all-important elements. It has permitted us to establish the different matrices under which a specific transaction fits. That particular budget category automatically sends the appropriate information into respective accounts. This is, therefore, the scheme of integration which has permitted us to succeed in having the system function.

Since 1992 to the present day, we can divide system development into three different periods: a period of implementation, a period of dissemination and a third period of consolidation, which is where we are at this point in time. Currently, we are in the process of integrating the management of purchases and sales and collection of taxes. We are now looking at the utilization of resources. We can open an account and capture all of the information. At any rate we can get to the various kinds of aggregations. A review of these accounting matrices is the first step in developing cost accounting of all public services. We have information about the cost of each one of the services involved.

These are the technical aspects and phases that have permitted us to develop the consolidation and integration of the system.

Thank you.

Jim Wesberry, Casals and Associates
Director, Americas' Accountability/Anti-Corruption Project

Thank you Alberto. Another quick anecdote. If I were writing the history of the last 20 years of international financial management, there are two reports issued by GAO which provided the incentive to USAID and other donors to get active in this field. Twenty years ago, I met Jim Hamilton, who is up here in the front row. He was a staff auditor with GAO. He came to Ecuador where I was working at the time with the GAO team which did a study on the importance of financial management to development projects. He recommended to the administrator of AID that it convene the other donors to talk about putting more emphasis on financial management in international assistance. Jim was a member of that team, not a director, but that was a historic report. Five or six years later, when I was back in Washington at GAO, a colleague at GAO who is over on the other side of the room, Lynn Moore, was head of a team which did another GAO report on the importance of training in financial management for the success of international development projects. Those two reports, more than anything else, led to the activities of USAID and a lot of other donors.

Now, Lynette Asselin is going to talk to us about the Inter-American Development Bank and its projects.

Lynette Asselin, Senior Financial Management, Inter-American Development Bank

My presentation is probably the shortest, and hopefully the most general presentation in this group. The theme of the conference is The Past 20 and Next 20 Years of Governmental Financial Management. Since this is such a trendy conference, I decided to change my theme a little bit to The Trends in Financial Management, i.e., what have we seen in the past, what have we learned, and where are we going in the Year 2000.

To begin, I would like to show what the international donors or financing organizations were doing in the Americas at the end of the 1980s. They had $177 million committed to the area of fiscal management. I use fiscal management because, in the Inter-American Development Bank, we include tax, customs, financial management and audit. This figure, $177 million, represents USAID, World Bank and the IDB. In 1995, the amount had doubled, as had the number of countries. By 1997, $374 million was committed to improving revenue collection and financial management.

Where are we today? The Inter-American Development Bank has $1.8 billion committed to this effort in the Americas. Twenty-two of our twenty-six member countries have some type of financial management, tax or customs reform going on at this time. The only four that are not currently involved in a project with the IDB at this time are Barbados, Belize, Chile and Jamaica, although they have had projects, and I know Jamaica is currently working with the World Bank. So, almost every country in the Americas is doing something in this field.

This is a breakdown of the member countries and what is being done. The yellow line represents 1996 and the pink line, 1998. In the case of Argentina, which has projects at the national, provincial and municipal levels valued at more than $400 million, and Brazil with a $1 billion project at the subnational level, I have omitted these amounts in order to see the comparison among the other countries. If you discard those two countries, you can see the enormous growth of investment in countries like Columbia, El Salvador and Peru, in this area.

Of the nearly $2 billion that the IDB has committed in this area, you can see that we work in customs, financial administration and integrated projects. What is an integrated project for us? An integrated project is a Reform of the State project, with a capital R and a capital S. This means that the reform may include civil service reform; perhaps decentralization. The reform may include many components, but at least one and probably all three of the fiscal components are also part of that package.

The last chart shows both the country's commitment and the IDB's commitment. What kind of projects do we do? How are they funded? One of the interesting trends that we see is that our Bank uses both technical cooperation and sectoral loans. Technical cooperations, in the past, have generally been non-reimbursable. What we see is that more and more countries are willing to take out loans to support these efforts. This is commitment on the part of the governments, and they are investing more and more every year.

Now, this is not a very colorful chart, and it looks like just a bunch of countries and a bunch of projects. But, if we look carefully, we can see several trends in this chart. If you look back to the period of 1992 to 1994, most of our projects were in customs or tax. The World Bank, AID and IDB had just begun to enter the financial management area with Nicaragua. Peru began an enormous Reform of the State project of which an integrated financial management system was a part.

In 1995, in financial management, we only had two very small projects. The one in Suriname created a financial information unit, and the other project helped to simplify the administrative procedures in the Finance Ministry in Guatemala. But, looking at our chart, as we move toward the right, we see more and more investment. In 1996, El Salvador and Columbia became involved in financial management projects. In 1996, the Bank started to get involved in subnational projects; up until then, it was always central government projects. The other thing the chart shows is that Argentina and Brazil, being larger countries, were committing more and more, both at the national level and at the subnational level.

The beginning of our investment increase was in 1997. In 1997, Columbia began a project to share information among departments and decentralized agencies, and strengthen the government entities. A loan was signed with Costa Rica to help them to privatize and strengthen their central financial management system. That project is still in the pipeline. In 1997, in the Dominican Republic, Ex-Vice Minister of Finance Ricardo Gutierrez from Argentina did an assessment, and helped them design the larger program which would lead to the loan in 1998 for a full-blown integrated financial management system. We're helping Mexico in public credit. We're helping Panama in the Treasury area. Panama began in 1992 under an AID project with five or six consultants. They've been developing their integrated financial management system, SIAF-Panama, and on October 1, 1998 the system was declared the official financial management system of the Government of Panama.

The year 1997 also marked our first entry into helping audit offices. Why is this important? When you talk about the World Bank, the IDB, Asian Development Bank or any of the regional banks, our membership is made up of Ministers of Finance from the executive branch who aren't always that enthusiastic about strengthening the audit or evaluation function. This is changing; there is tremendous growth in this area. This year we have three new projects for which the executive branches in the Dominican Republic, Haiti and El Salvador have agreed to sign for a loan to strengthen these audit institutions.

So that is where we are. What have we learned from these experiences? As Mauricio Mathov mentioned, a group of people got together in Peru in May, and we talked about what we learned. We're talking about millions of dollars in investment in improving financial management and audit. The first thing is the political aspect. I've had people say to me, Oh, an integrated financial management project, it's technical. It's not political. That could not be further from the truth. There is nothing harder than convincing people to change their ways. And time and time again if you don't have that support at the top level, your project is stalled.

In one country, for two years, the Vice Minister of Finance was really not interested in the financial management system. There was a wonderful group of technicians over there working away to develop the system. They went to the Vice Minister and they taught him how, if he turned on his computer, he could see how much money he took in that day, and how much money he spent that day. The man is like a little boy with a toy today. So much so that they signed a new $1.5 million loan to finish implementing the system this year.

On the other hand, I also visited a country where the Minister of Finance said to us, That's fine. Love to have your system. But I really don't want to work at it. I just want the millions of dollars of economic support. I don't really need your technical cooperation. Nonetheless, for political reasons, that loan must be approved. How do you deal with this type of reality? How do you start a project when you know, from the beginning, you don't have that support? Anyone who has some answers for that, please share.

Another thing that is extremely important in the political area is public awareness, not just from the government employees, but the citizens. Raise awareness. I've been in places that are in the middle of a reform and neither the people in the organization nor the citizens can tell you what is happening. More and more, we have identified the importance of making the people that have to go through the change a part of the change. One of the best places in the world to see the importance of this concept was in Buenos Aires, when they were doing all the internal audits of the privatization and publicizing the results. Citizens felt good to know that someone was monitoring those privatizations. It is extremely important that awareness is part of the program.

I challenge anybody to facilitate the process of international financing. The lesson learned: only one donor, only one bank. If you have three banks, you have three agendas and three reporting requirements. All three know where they want to go, but it is usually in different directions. Only one. And if you have more than one, you need some kind of coordinating mechanism that does not favor any of the three.

Modernization of the State reforms are huge, huge undertakings. Financial management is often part of modernization of the State, and it is extremely important that the framework of modernization includes financial management.

Mauricio and I worked together over in Africa for the World Bank. This African country first had a project in civil service and it was wonderful. They got a whole new group of computers. They cleaned out all the outdated information in terms of their personnel and civil service. The problem occurred when another project in financial management came along, and the Civil Service Commission didn't want to share the information, even though the Ministry of Finance made the personnel payments. So, it's really important that all of it go into this big framework called modernization of the State, and that we all work together to coordinate it.

Again, I'd like to challenge you to agree or disagree with the following points, or tell us how you treated these things, because they are things that constantly come up whenever we're planning a project.

Clear objectives and goals based on reality. There is no one right way for every country.

Acceptance and sponsorship of the project by political authority. We all know how difficult that is. Power is a big thing, and to create a win-win situation for everyone is difficult.

Adequate and realistic planning of the project. We find time and again it is so easy to say, Oh, yes. We'll do A, B, C and D. Then, of course, you come in a year later and, Well, you know, we did B and maybe C. Start at the beginning. Don't make unrealistic expectations. Just because country X could do it at this rate doesn't mean that you will do it. As your teams plan it, think of the reality. Think of what can be done, and in what time frame.

Opportune time to begin. This comes down to, and we've all run into it, elections. Do not start a major reform a year before an election. It doesn't work, because every time there is a change, there will be changes. It is not good or bad. It's change. You have to plan carefully, taking into account who the players are going to be. If the entire group is going to change in 12 months, you have to look at, What can we do that won't be thrown out with the bath water at the end of the day?

Optimal relationships between international and national consultants. You know, international consultants aren't saints. They don't walk on water. They may get paid more, but their job is to come in and share experience. Therefore, the relationship is extremely important, because, remember, the international consultants will leave.

Organizational responsibilities. Define and apply the proper organization to the individual project requirement. Every project may have a different structure. Choose one. Define the one that is best for your reality.

Institutional support is self explanatory.

Adequate mechanisms to guarantee the sustainability of project results.

Technology compatibility. Again, you bring in these wonderful people and they develop systems in FoxPro. Today, that technology isn’t transferable. How do you make these decisions not knowing what is going to be the technology in three years?

Adequate legal support for the recommendations. There is an ongoing debate, Do you need the law before the project or after the project? Bolivia had it before, Panama still doesn’t have one. I don’t know. I leave it up to you.

In conclusion, where are we going? In the future, there are a couple of areas that I see us moving into and exploring at this point. There is an increasing debate on fiscal decentralization and its impact for revenue as well as expenditure. Decentralization is a huge movement. How is it going to impact fiscal management? Are our models going to work? Will the models that we’ve developed at the national level work at the decentralized level? As someone said earlier, maybe it’s better to start at the decentralized level like they did in Ecuador and move toward the national. We expect to see a continued growth in financial management reform projects at the municipal, provincial and Federal level.

There will be a continued emphasis on transparency and accountability. Whenever we go to a country, we use the IMF’s new Code of Good Practices on Fiscal Transparency and other things. We see a growth in support for Auditors General and Controllers General that wasn’t there five years ago. Also, as a Bank, we have worked with CAROSAI and OLACEFS, which are the regional audit organizations, and we will continue to do so.

Lastly, what I see, as we go toward the Year 2000, is performance measurement. People are going to say, Okay, we’ve invested millions. Are we really making a difference? I think we’re going to have to come up with a lot more evaluation models to support where we’ve been and where we’re going. Hopefully, we will be able to quantify and qualify things, and prove to ourselves and the world that all of this has been worth it. Thank you.

Jim Wesberry, Casals and Associates
Director, Americas' Accountability/Anti-Corruption Project

Thank you, Lynette. Now, we've promised you a panel and we have got the panel up here before you.

Another quick vignette from the history of the International Consortium. When the Consortium was formed, the Comptroller General of the United States was Elmer B. Staats. The Auditor General of Canada was J.J. MacDonnel, both very dynamic, towering people who made history. Elmer Staats, introduced broad scope auditing, and Mort Dittenhofer's Yellow Book of Auditing Standards, and many other things. MacDonnel introduced comprehensive auditing, reforming auditing in the United Nations, and finally acting as Auditor General, he formed the Canadian Comprehensive Auditing Foundation, which stands as a monument to his memory after his death. Elmer Staats is still living, but is unable to attend meetings like this. He is our honorary Chairman Emeritus of the Consortium.

The next two Comptrollers General were Charles Bowsher of the United States and Kenneth Dye of Canada. Both of them were at our first conference 14 years ago, and were speakers. Kenneth Dye is with us. He will be introduced to you tomorrow. Charles Bowsher called me the day before yesterday. We had given him a special invitation also to be present. Mr. Bowsher is receiving an award in Chicago and could not come, but sends his best wishes for the success of this conference.

I have a question for Maurico Mathov which concerns me, and I keep asking this all of the time. Why is it, Mauricio, that we cannot have a single, packaged software package like SAP or Peoplesoft in the private sector that governments across the world can use for integrated financial management? Also, we have an illustration of something that works, the SIGADE system developed by UNCTAD, that is in use in about 40 countries in seven or eight different languages across the world. It is a packaged system, but only for debt management. Why can't we do that for all of financial management?

MR. MATHOV: I think that in theory what you are saying is feasible. The problem is that each country feels that its own problems are different from everybody else. In my experience, that is generally not true. But that's the way they feel. And since they are not here, I can't speak for them. I went for the World Bank to see an integrated financial system in two states in Russia. Both were different systems with different problems because each state felt their operations were unique. I told them about this conference that's held every six months. Why don't you come here and see what other government problems are and maybe you will see that your problems are not all that different. They never came. They are not here. They were not here six months ago or a year ago. So each government wants to think that they have different problems than the other governments.

MR. WESBERRY: Any other questions or comments on that? Is there any software manufacturer present that would like to make an offer?

MR. HUGHES (United States): I'm not a software manufacturer, but I do have a question. I was very interested in the presentation from Argentina relative to the reconciliation made between the government accounting numbers and the macroeconomic systems of accounting. Could you expound on that, and is that just in your country or is that in general throughout the Latin American countries?

MR. AROLFO: The conclusion that one can make from the manuals of the United Nations or International Monetary Fund is the need to go to a single system in which the accounting aspects of the government and the accounting aspects of the different companies within the private sector are involved and are committed together within a big macrosystem of general accounts. In Argentina we automatically roll up in the national accounts, the production accounts, the income accounts and expenses of everything that has to do with the public sector. But while this is an experience that we have developed, I don't think there's any problem in developing it in other countries.

MR. ALBANO: I am going to comment also from the point of view of Guatemala. My comment concerning the council is basically that the integration of these systems is not just automation. It is a concept. Once we have integration of the concept, all the classifiers included within the integrated system, administrative classifers accounts, accounting classifers, etc., all these have integration in themselves. In the case of Guatemala, we presented this project on September 2, 1998. We had the national budget presented to Congress. This budget project, which was presented in multimedia, something new for us, has an entire process of integration from the minimum programming that exists in a transaction to the information provided at the level of a ministry or in a sector of the economy. We can have the information at the source of finance at the regional level and at activity sectors in the public sector. At the same time, since each classifier was developed on the basis of the United Nations Accounting Manual and the IMF Statistic System, we can integrate the public sector through the national economy. We're talking about an integrated system and concept. The computers just give us the necessary tools to do this in an acceptable period of time, so it can be used for decision making. The system we have in Guatemala for formulating our budget is also used in executing our budget. The system works on real time. At any given moment, we can produce the balances of the State. We can produce accounts on how we have invested and we can project the investment on the national guarantee.

MR. HAMILTON (United States): This is along the lines of what we heard from Maurice Mould this morning. I think one of the challenges he said that we'd be facing in the next century is integrating the accounting information with the macroeconomic data. And I see some of this transpiring here in Argentina and in Guatemala. And it fits in with a conversation I had with one of our economists. We have these general data standards that we're trying to put into a system throughout the world to capture the national account data. And I said, Can't you use the data that the Controller General produce? And he said, Well, it's the right data, but it's classified a different way. It is classified around different kinds of functions that are legislative, but our data is classified in other ways and collects all of the expenditures in a general area private and government. I'd like to ask the panel: Is this, as Maurice said, one of our challenges, to bring data systems that capture data in various manners into sync?

MR. AROLFO: Our challenge, and this was the reference of framework that we had in Argentina, was to consider all of the mechanisms for information in order to obtain the macro amount of figures concerning public accounts and national accounts. Specifically, this was one of the objectives that we had in developing the infosystem, to point out the need to obtain this integration. Because, as was said by Mr. Albano, this is a conceptual integration. When we talk about conceptual integration, we have to make all the technical languages the same. We need to develop budgets in the same way. There should be similar accounting techniques, and public credit procedures, and even the treasury operations should be the same. Once we have conceptual integration, we can truly obtain the information we need for sound financial management.

Financial Management and Reporting in Century 21

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Thank you all for spending the last part of today with me as we talk about the subject of financial management and reporting in the 21st century.

This is a list of the topics that I will cover. I'll start by getting a little perspective about the past, the earlier centuries. Next, I'll come up to the end of the 20th century, current times. I want to talk about some major megatrends that I think are going to influence where accounting, financial management and auditing are going in the 21st century. Then, we'll talk about some specific predictions for the 21st century.

Let's start with the past. Accounting, I like to say, has a very glorious past. Going back a few hundred years ago, accounting was the necessary infrastructure that allowed large-scale enterprises to form so we could have an industrial revolution. Without the technology of accounting, large enterprises couldn't be controlled and managed. They couldn't handle measurement and communication, planning and decision making. They couldn't fulfill their accountability responsibilities. For all these reasons, having this accounting technology in place permitted the Industrial Revolution to take place. Then, as ownership and management became separated from each other, a modern auditing profession came into being and improved the credibility and reliability of these accounting reports.

You put all that together and you get a considerable set of benefits from modern accounting and auditing. First of all, it permits these organizations to plan and control their activities. Secondly, transparency in accounting reduces capital costs for enterprises because it reduces the information risks to investors and creditors, which allows them to reduce their demanded returns. That's a huge benefit. Providing a lot of high quality information to buyers and sellers of financial securities means that bid-ask spreads can be narrowed, transaction costs can be lowered, and there is more liquidity. So transparency in accounting adds liquidity to financial markets. Financial resources can flow to their best uses. Put another way, allowing transparency facilitates capital flows and economic efficiency and permits the conditions of market trust to form, so that people are comfortable dealing in financial markets. That's where we're coming from in the past.

Now I want to come up to the present and talk a little bit about where that leaves us. A couple of months ago, I picked up the June/July issue of *Foreign Affairs*, a journal that is heavy on foreign affairs, international relations, and so forth. You would expect that a journal like this wouldn't have very much to say about accounting. As I read through it, I found quite a few references to accounting. I want to share them with you because they provide some perspective. All of these quotations are from that single issue of *Foreign Affairs*.

In an article on Japan, the author said, Meanwhile a variety of other gimmicks appeared to improve balance sheets and thereby prevent public recognition of weakness or insolvency. The author was making a direct connection between lack of transparency in financial reporting and problems in the financial marketplace. That's a perspective from Japan.

Another article focused on India. That author said, Retail investors are scared away by the stock market scams. The resulting high cost of capital makes Indian industry and exports less competitive. So, because people don't trust the markets, Indian industry is less competitive.

Another quote from the same issue of the *Foreign Affairs*. This one relates to Russia. This author says, Open accounting that meets international standards is a prerequisite to controlling corruption. That's another take on it. If you have lots of transparency and high quality information, it is more difficult to have corruption in the financial markets.

Yet another quote from the same journal. This one refers to the United States, but it's last century. It's in the 1900s. The author says, The United States economy between the Civil War and World War I was notoriously crisis-prone. Nor were catastrophes like the panic of 1873 pure accidents. They were made much more likely by a business and political culture in which petty things like scrupulous accounting were disdained. That means bad accounting contributes to financial panics and other problems.

Compare that with this last quotation I'll cite. Again, this is the United States, but coming up to the 20th century. This author says, Unlike the Asians in particular, Americans know more or less what is being done with their money. Accounting systems in the United States strive for clear corporate information. No other country's financial system reflects such a willingness to bring financial problems to the surface.

These quotations are not accountants talking to accountants, not financial managers talking to financial managers, but people who think about international relations and foreign affairs talking to each other and citing accounting issues as important issues in international affairs.

That's just a very brief history. It brings us up to the present, ready to look at the future, which is my assigned topic. I want to focus on some megatrends. These are the huge overarching trends that are going on in the economy and which I believe will affect the way accounting and auditing goes in the 21st century. Here are the megatrends on which I really want to focus.

First I point to a worldwide increase in demands for accountability. Everywhere you look, people are less and less willing to place trust in institutions the way they formerly did. They distrust governments. They distrust religious leaders. They distrust universities. They distrust the professions. They distrust business enterprises. They are demanding more and more accountability from these organizations in order to get a better fix on what they are getting out of these organizations compared to what they are putting into them. We see this everywhere in the world. Increasing demands for accountability is a megatrend.

A second megatrend is information technology. That's very obvious, but I want to dwell on it for a few minutes. Then I'll talk about how information technology is shifting power relationships in the marketplace, and I'll wind up the megatrends by telling you how I think that they are leading to the obsolescence of our current accounting models.

Let's start with the information technology area. Everybody knows about this, but I want to make sure we're all at the same point. Everybody knows the operation of Moore's Law, the one that states that the chip density doubles every 18 months. Every 18 months, you have twice as much power. At the same time, the costs are not going up; they're going down. So, all the components of information technology, by which I mean the central processing units, the memories, the communications links, and the sensors that relate the real world to the digital world, are all getting smaller and cheaper all the time. As a result, they're becoming ubiquitous.

For example, when you start a modern automobile up and turn the key, you're probably activating 10 or 20 microchips and more than 100 sensors sensing things like the thickness of the brake pads, the air/fuel mixture going into the engine, the pollutants coming out of the engine, the status of all the systems. Because the costs and size are going down, you're getting a lot more deployment of this equipment and the power is going up enormously. Everybody knows that. There are people in this room today with more computing power on their wrists than was used to send Neil Armstrong to the moon 30 some years ago. As a result of this, you basically have an ubiquitous network emerging over the last couple of years where virtually everybody in the world with a PC can be connected. Information is available any time, any place. The potential really is here to have a complete office in a briefcase. That's today.

If you project these trends for more power, smaller size, cheaper equipment, it's easy to see that whatever we have today is going to be available in much more profusion in the future. It's going to have enormous implications. What happens is that these technology trends lead to a type of power which has meaning only when that power is put to use. What I'm talking about is the use of this technology to achieve business objectives. What happens is that the leadership companies in an industry figure out how to use information technology to get strategic advantage in the marketplace. They do things like getting closer to their customers. What do I mean by that? Let's say that a customer has a need for something at a certain time and place. And various vendors are able to meet that need at various times and places. The vendor whose cost and quality can come closest in time and space to meeting the customer needs is the one who will get the business. Competition is about reducing time and space differences between the expression of needs and their fulfillment.

Let's look more closely at what information technology is about. The computing part of it is about crunching time. So computations that used to take months now take nanoseconds. Computing crunches time down and communications networks crunch space down. They collapse space by permitting organizations to operate globally. Information technology is used to reduce time and space and that is exactly what is needed in order to serve customers. Information technology isn't just a tool used in business; it is a tool to create competitive advantage. These leadership companies use the technology to get closer to their customers, to demassify products and services.

What do I mean by demassification? A mass product or service is a sort of one-size-fits-all model. Henry Ford, who put America on wheels, was famous for saying that you could have a Model T Ford in the color of your choice as long as it was black. There was no choice. If you wanted to ride around on wheels, you had to take a one-size-fits-all product. But when a vendor makes a profusion of products available and people can select something that better meets their needs, that vendor is going to prevail over vendors that provide one-size-fits-all products.

Another example in the information area: newspapers. In the United States, we read the Wall Street Journal to find on what's going on in the financial markets. The Wall Street Journal is a one-size-fits-all product. The editor gets all the news feeds. The editor decides what to put in the newspaper. You get that newspaper and you can take it or leave it, one size fits all. Now, through the use of technology, you can log onto the Dow Jones web site and you can look at all the news feeds that the editor of the Wall Street Journal sees. You can decide what to read. You can design a daily newspaper for yourself that is different from every other one in the world. That's another example of demassification through the use of technology.

I could give you lots and lots of examples like that, but I think you get the idea. Business leaders use technology to demassify products and services, and thereby have a competitive advantage. They also use technology to improve the quality of products and services, to figure out how to identify defects in the product or defects in the production process, and design those defects out so that their products have higher and higher quality year after year. Of course, they also use information technology to go global, so that a single enterprise can really deal around the globe, something that was not at all feasible a generation or two ago. Now with modern technology it is quite feasible, and the leading companies are global.

Those companies that aren't strategic leaders have two choices. One choice is that they can catch up. They can try to figure out how to use the technology themselves to do things like emphasize product and process quality, decrease the cycle time in getting products to market, focus on the creation of value for their customers, go global, downsize or get rid of the fat in their organizations. They can go into partnerships and alliances with others to pick up missing technologies and people skills, and make strategic use of information technology themselves. The other choice is to go out of business. Avoiding the use of information technology is incompatible with survival in the modern business world.

Having said that about business and industry, I want to turn the spotlight on accounting as we get closer to our own domain. What I will assert to you is that the accounting models that we use in the United States, generally accepted accounting principles, were designed to describe an industrial enterprise that creates value by the manipulation of tangible assets. An industrial enterprise is one that takes in raw materials, applies labor and energy, and turns out finished goods. The financial statements show those tangible assets that are used in that industrial process. They show the raw materials, work in process, finished goods, machinery, equipment, buildings and land that are used for that physical process. That's what's in the financial statements.

Because of information technology, more and more enterprises are becoming what are described as post-industrial enterprises. They've slipped into a new paradigm, one where wealth creation is less and less about the manipulation of physical, tangible property, and more and more about the creation of knowledge and the transmission and use of knowledge. The typical post-industrial enterprises' key assets include the capacity for innovation, knowledge about their customers, information about the marketplace, a committed and creative work force, good relationships with vendors and customers and employees. These are intangible assets that are not reflected on the balance sheet at all. I'm not suggesting that we put them on the balance sheet, but what I'm suggesting is that the balance sheet, by ignoring these key assets of the post-industrial area, does not describe these enterprises very well. We have to figure out what to do about that.

You're saying to yourself, But there are still plenty of people that are in the manufacturing business. How about them? Does the model describe them at least? Let me tell you that we still have people involved with tangible property here in the States. We like to eat, so we produce food. But only 2 percent of our work force is actually involved in growing things on farms. And we Americans like to drive around in automobiles. But only 10 percent of the American work force actually makes things in factories. On the other hand, more than 70 percent of American workers are involved in the production, distribution and use of information, and more than 70 percent of them are involved in the information sector. There aren't that many pure manufacturing companies today.

Even companies that are involved in manufacturing are looking more and more post-industrial. A manufactured good is something that if you drop it on your foot, you hurt yourself. It has tangible weight to it. Let's think about something like that. Take one of our American companies, like Motorola. They are a manufacturing company they make things. If you drop a cellular phone on your foot, it hurts. You go out and you buy one of Motorola's cellular phones. Let's say you buy the model that costs $100. So I ask you this question, Of that $100, how much of it is for things', or for the tangible content? I will assert to you that there is less than a penny's worth of sand in that telephone. There is less than two cents worth of copper in there. There is less than a nickel's worth of oil in there, which was turned into a plastic box. What's the rest of the $100? It is research and development, software, programming, innovation, brand equity, and all the soft assets. Even companies that look like manufacturing companies and produce products have more and more of an information component to them.

Another way of making the same point is that over time, the assets important in creating value are shifting from the tangible to the intangible. So, at the left side of this diagram, you can think of a steel mill. In order to produce steel, you have to produce lots of tangible assets, like blast furnaces, factories, and those types of things.

At the right side of that picture are companies like Microsoft and companies whose tangible assets are almost negligible and whose entire value-creation function is intangible. If you look at Microsoft's balance sheet, prepared under the accounting standards that the accounting profession prescribes, you won't find anything of interest on the balance sheet. There are a couple of desks and PCs, but let's face it, all of the assets that lead to a market capitalization of $300 billion are between the ears of Microsoft employees, all intangible assets.

What I'm suggesting to you is that industry is moving from the left side of that picture to the right side where intangible assets are more and more important for more and more businesses. And our accounting model neglects them.

Another way of thinking about it is that the product that we provide as accountants can be described with these five components. We have periodic, historic, cost basis, financial, statements. Periodic goes back to the agricultural era, where we summed up once a year. Since then, we've gotten that up to once a quarter. Inside the company, it may be more than that. Historical is looking backward, not forward. In cost basis, we show what the assets cost when they were acquired. Financial says that the numbers in these statements are denominated in monetary units, lira or yen or pesos or dollars or whatever. A statement is something that's boiled down from the extensive books and records of the enterprise.

This was a good trick when we accountants thought it up 500 years ago, a way of summarizing a complex entity on two pieces of paper one that shows its point in time position, a balance sheet, and another that shows what happens between two balance sheets, an operating statement or an income statement or a cash flow statement. The summary benefitted people who couldn't come into the renaissance or early industrial era enterprise and thumb through the ledgers and journals themselves to form an impression of the company. Instead, they could look at a summary of a couple of pages.

But look at each of those five descriptors and think about how people today demand information and how they receive information in every sector other than accounting. While we provide periodic information, they're used to the idea of logging onto the network and getting information on demand, whenever they want it. We provide historical information. What they want is information right up to the minute, and if possible, even looking forward. We provide cost-basis information, and they want to know the current value of the company's resources in order to make customers better off in the future. We provide financial information, and while it's true that they want the financial information, they want much more than that. They want to go behind the financial information and see the operating data that lie behind it and see the leading indicators that might tell where the company is going in the future. They want more information on risks and opportunities facing the enterprise, a much more comprehensive information set. And finally, they don't want a statement or a one-size-fits-all boiled down version of these balance sheets and income statements. Statements are general-purpose, meaning they don't really suit the needs of any particular user. They are a compromise.

Today, people are accustomed to the idea that they can log onto a network, get into a database, decide what information they need, decide what format they want it presented in, and have it brought to them in real time with the ability to drill it down and sideways and elaborate on their understanding of the enterprise. We're providing what's on the left side of the diagram. In every other domain, except accounting, people are used to seeing what's on the right side here.

As a result of these things, we accountants have what I would call in the private sector a loss of decision information market share. I've shown that here graphically. At the bottom of this picture you see the red area which represents the information that's conveyed by financial statements. The green area then is other information that's available to investors or creditors who are analyzing an enterprise to decide whether to put money into it. At the beginning of the century, a large portion of the information needed to make that decision would come from the financial statements. The financial statements were never all that you needed, but they were a lot of what you needed. We accountants had a relatively large share of the total information that was required for these purposes. As the century proceeds, financial statements do get better, because we had improved principles, improved standards, and improved education. But toward the end of the century, I would assert to you that the informativeness of financial statements is beginning to decline, and it's because of what I mentioned earlier. It's because the enterprises that we're describing have shifted from industrial to post-industrial, and the accounting model doesn't cope with that very well.

While what we're providing is losing its decision information effectiveness, decision makers can acquire much more information. In the middle of the century, low-tech information intermediaries emerged. In the United States it was firms like Moody's and Dun & Bradstreet and Standard and Poor's, providing lots of information about companies. Later in the century there was an explosion of information because of the availability of information technology, i.e., large databases, publicly available. Today when an investor or creditor is trying to decide whether to commit money to an enterprise, he or she can go out on the Internet and find out huge amounts of information that will help to make that decision. Sure, they use the financial statements, but the financial statements are a much smaller share of the information. So a difficulty that we have as accountants is that green area on the chart is one that we're not involved in producing or auditing. It's a loss of market share. It's getting away from us because we're not paying attention.

Yet another way to think about this, and now I'm framing it the way an auditor would, is that a company with either debt or equity has a requirement to prepare general purpose financial statements. An auditor audits those statements, and his or her opinion goes on the statements, and then they go out to some user. That's the picture as we see it. We issue an opinion on the financial statements, and they go to investors or creditors.

I ask you, What's wrong with this picture? I can list three things that are wrong with this picture. The first one is that decision makers have many other sources of information that aren't on the picture. A second thing we find is that typically the audited financial statements arrive after the investment or credit decisions have been made. That's true for both debt and equity investment decisions. The audited financial statements only have a sort of after-the-fact confirmatory role. Other information is actually used. The third thing that's wrong with it is we're showing here a producer-driven, general purpose, one-size-fits-all product, as I've already mentioned.

I want to digress and talk about one of the implications of information technology. It has this effect of shifting power in the marketplace from the producers of goods and services to the consumers of goods and services. We had producers and consumers in the industrial area, and the person who decided what the products and processes looked like was the producer. Henry Ford was the one who decided how many horse power went into the automobile, where the driver sat, and what color the car was. All you got to decide was whether to buy it. Henry Ford had all the power to determine products and processes in this model. That was generally true in the industrial era. But information technology inexorably shifts that power from producers to consumers. Once there is differentiation in the marketplace and consumers can vote with their money for the products they like, they acquire the ability to determine what the products and processes look like. If they don't see something in the marketplace that suits them, they have the ability to force the marketplace to meet their needs. This demassification of goods and services shifts power to consumers. The consumers are now in the driver's seat and determining what products and processes look like.

Keeping that in mind, let's redraw that picture of the financial statements and the audit report going to the decision maker, and let's redraw it like this. What we're going to do now is think not about those arrows going out from the company to the decision maker, but rather about the decision maker deciding what he or she wants and issuing demands for information. So the arrows are going from the consumer, who has the power, to the enterprise. The decision maker is now in the commanding position to issue demands for information. The enterprise is going to have to respond to those demands and supply the information in real time.

Now the decision maker, the consumer, has the information but doesn't know if it's any good and is going to issue a demand to the auditor for assurance about whether the information is reliable. The auditor is going to have to figure out how to respond to that demand in real time and provide the assurance back. Online, real time assurance. What you get is a very different picture. It's not the picture of issuing one-size-fits-all financial statements once a year or a quarter. It's a picture of decision makers demanding the information they want, issuing a sequel query or some other form of demand which is run in real time against relational databases and back comes the answer immediately. Those people are going to want to know if that information is reliable. If auditors can't provide that information on reliability in real time they will be replaced by somebody who can do that.

Let me turn now to the 21st century. I'm going to make three sets of predictions. First, I'm going to make some predictions in the area of financial management, then financial reporting, and finally some more general but, I think, relevant predictions for us as accountants and financial managers.

Financial management. I may be using it in a somewhat narrow way here. I'm thinking not about all aspects of financial management, but about the information systems inside an enterprise or governmental unit or what have you. I would say that the term management or managerial accounting that we have used for many years is an obsolete term. It's obsolete for two reasons. The first reason is it doesn't provide any information that managers want. Managers of an enterprise are not really interested in the transaction flows at the detail level. What they're really interested in is organizational transformation. They need information that tells them whether they're achieving their strategic objectives. So-called management or managerial accounting systems don't provide that information. What they provide is the summarization of transaction data, which is of interest to the enterprise but not to the managers. It is of interest to those who are actually undertaking the activities at the lower levels of the enterprise. The person who needs this information is the clerk out on the front line who is dealing with customers or the product person on the production line who is actually moving the manufactured goods through the process. It's the rank and file in the organization who need the information. So these managerial accounting systems need to be substantially changed to support everyone in the organization, and we need to think very differently about what information management needs in transforming the organization.

Another problem is that people are tired of getting lagging indicators, which is what we accountants typically provide after-the-fact indicators. Let me, before I go on to the corporate dashboard, tell you what I mean by a lagging indicator. On this slide I'm showing cash flow. Once we have cash in the bank and all the transactions that result from that have taken place, we know where we wound up, with cash in the bank. But if you were trying to think about what cash we would have in the bank in the future, you need some leading indicators.

Here are some leading indicators. If you have satisfied customers, then you'll probably be making more sales and more cash in the bank. If your customers are dissatisfied, then your cash flow will be going down. So customer satisfaction is a form of information that would be a leading indicator. But what indicates customer satisfaction? The leading indicator for that is high quality products and services. Well, you say again, what is the leading indicator for that? The answer is high quality processes, manufacturing, design, and so forth. And before that can happen, you have to have a committed, disciplined, intelligent, educated, and motivated work force. So each one of these represents something that is a conditioned precedent. You can think about them as a set of leading indicators. Any one of them could be the subject of measurement in an accounting system that would permit you to think into the future, not just into the past. That leads me then to the idea of the corporate dashboard.

This notion is also sometimes called the balanced scorecard. The idea is that when you're driving an automobile you don't just have one gauge on the dashboard. If you had just a speedometer, you wouldn't know when you're running out of gas or when the engine is overheating, or the electrical system isn't charging. That's why you have a set of gauges on the dashboard. That's the reason for talking about this dashboard. It's a set of indicators that covers a number of different important functions.

Now what set of indicators would any enterprise have? The answer to that depends on what they are trying to achieve. Let's use a generic example, which in this case is to be rated number one by our customers in total value delivered. A real company would have a much more specific vision. Then you ask the question, Okay, if we succeed in achieving that vision, how will we look to the people who own us, the shareholders? So we need a set of gauges to answer the question. The gauges might have names like a profit gauge, or an income statement, a growth gauge, and a gauge that shows what's happening to stockholder value. Is it going up? Are we creating value? Or is it going down, and we're destroying value? It's possible, as you know, to have positive income and still destroy shareholder value. These things measure really different aspects. The types of indicators you might have are market leadership, high revenue growth, and profitability indicators.

We accountants already provide this type of financial information. That's good, but now we have to think about leading indicators. What is going to indicate those financial results? The leading indicator that comes before that is a happy customer.

How do we look to our customers? We need a set of gauges associated with cycle time and product or process quality and service to customers. We might be measuring things like lead times. We want superior lead times, low defect levels, on-time delivery, and responsiveness to customer inquiries.

We can get a set of internal measures that tell us about product and process quality. Such quality depends on a committed and capable work force. This in turn depends greatly on how the organization learns and improves. That's about human resources. And so we have gauges like innovation and continuous improvement and the development and maintenance of intellectual assets. What I'm suggesting to you is that a good corporate dashboard would have gauges for all these types of things. The specific gauges would depend on the specific company and what its strategies were. There would be measures in place to measure the achievement of those strategies.

The point is that no single gauge, such as an income statement, is sufficient. Of course, in government that's well known because there is a whole set of different activities that have to be monitored and the outputs of government are not all in financial terms. They are in production and welfare and social benefits and what not. So this idea is better developed and understood in government. The business world is in the process of doing that. What you see is big companies installing these balanced scorecard systems not only to provide the lagging indicators of the accounting numbers, but to establish leading indicators to get a more comprehensive view of the enterprise.

Based on what's going on in the way in which enterprises account to the outside world, I would say that the term financial accounting is also an obsolete term. It is obsolete because financial information is not sufficient. We need to move toward a new model. The American Institute of CPAs a few years ago had a blue ribbon committee named the Jenkins Committee after its chairman that studied where financial accounting should be going and made a whole set of recommendations. One of the recommendations is that we stop even calling it financial accounting because that's too narrow. It should be called business reporting. It should include the financial information, but it should include much more. Specifically, what that Jenkins Committee recommended is a business reporting model with 10 components.

Several of the components relate to standard historical information, the financial statements, and operating and performance data. A more innovative component is management's discussion and analysis to help users understand what these numbers and disclosures mean. Then we move into the future. We want to know what the company's opportunities and risks are. We want to know at least at some level of detail what their plans are. And to the extent they tell you about their future plans, there should be a reconciliation. When a period goes by, we want to know how the company did or how close it came to meeting its plans.

Another component is relationships. What other companies relate to it? Directors are interlocking with other organizations to make some assessment of how well their relationship is working.

All these components constitute an extended information set called a business reporting model. Think about it this way: On the vertical dimension, divide information into financial and non-financial information, and on the horizontal axis, past and future. In the lower left corner we have financial statements, or their financial history and their past. What would be in the other quadrants? In the upper left would be the operating data that lie behind the financial numbers. In the upper right would be leading indicators, forward-looking information. In the lower right would be explicit financial forecasting. The Jenkins Committee recommended against that partly because of concerns about litigation. Companies that made forecasts and didn't achieve them would be subject to being pursued by litigation.

Now let's consider some predictions about connectivity, the transparency of organizations, and what's going to happen about capital costs. Then I'll conclude with a more modern definition of accounting than the one we're currently using.

First, the idea of connectivity. Enterprises are more and more related to each other electronically. On this chart I have a value chain. That's an enterprise in the middle. Its suppliers are on the left, and the customers are on the right. More and more they're being linked electronically. In the first place, they do that to reduce costs. What happens then is you use this electronic linkage to wring slack out of supply chains and make them much more efficient.

I predict that the capital suppliers of the enterprise will also be electronically linked. They are just one other class of supplier, and they will be electronically linked. Many companies in the United States say they will never do this, that they will never let their investors and creditors electronically link to their information in real time. That's what they say.

However, I point out to them that 10 years ago they said they would never let their vendors link to them electronically and get into their production databases. And yet, today, most big companies will not even deal with a vendor who can't link to them electronically. The reason they will link these capital suppliers electronically is it will lead to lower risk for the capital suppliers, and they will pass that back in the form of lower capital costs. That, in my opinion, is highly likely to happen within the next five to ten years in the United States and maybe sooner. It is true that companies don't want to disclose everything. For one thing, the more they disclosed to their capital suppliers, the more they were inadvertently disclosing to their competitors. There is no reason they should be forced to suffer competitive disadvantage. So the answer is to shield particularly sensitive information.

A second objection is that lots of the information in financial statements is not cut-and-dried. It really requires judgment. The answer would be to provide access to more factual information, not the judgmental information like the estimate of collectibility of receivables.

A third objection we sometimes get from companies is they don't want to put the information out there before they have had time to scrub it, in case there should be errors. They might be subjected to liability for inadvertently disclosing erroneous information. They need to revamp their systems so that they're much more resistant to error in the first place.

I think these things will happen. The results will be very beneficial to companies in terms of reduced capital costs. On this slide I've indicated the components of capital cost for a hypothetical company. The green bar represents the amount the company would have to pay if there were no risk. There are no risk-free companies.

Companies have to pay a risk premium because they are in a risky business. There is a premium for economic risk. There are also three other components of capital cost. One is an information risk premium, meaning the less that investors know about the company, the more they have to charge you for money to compensate for that risk. Of course, there are transaction costs in order to get public equity or debt. You'll have to pay lawyers and accountants and underwriters. You'll have to publish annual financial statements that are audited. So there are annual maintenance costs.

The interesting thing about the top three costs in this set of capital costs is they're information costs. Information technology is driving information costs down. I think what will happen is, holding the risk-free rate and the economic risk constant, the other three components, the information risk components, will all decrease as a function of information technology. This will lead companies to lower capital costs, which is a huge advantage to them.

We can think about capital costs as a function of disclosure. On the vertical axis, what I've shown here is cost. These are the costs to the enterprise to rent capital from others. On the horizontal dimension, what I'm showing is the extent of disclosure. On the left, no disclosure. On the right, complete transparency. They show the world everything. These two costs don't vary with disclosure. The economic risk premium and the risk free rate of return are not affected by disclosure. But then there are a set of costs that are affected by disclosure. I've shown them here in orange. That's the information risk premium. If we don't tell the investors anything, they charge us a big premium because they don't know the true facts. The more we tell them, the less the premium. If we tell them everything, there is no information risk premium. That declines with disclosure.

It's clear that the optimum disclosure would be to tell the world everything. Don't hide anything. However, there are costs involved with disclosure.

The more we tell the world, the more it's going to cost us to gather and transmit that information.

Then there is a competitive cost. The more we tell the world, the more our competitors benefit from it. They use that to our disadvantage in the marketplace. So there is a cost there.

Finally, there is a litigation cost. If we don't tell anything, and the company isn't successful, we're going to get sued for sure. If we tell them the true facts, then we might get sued, but at least we could win. The litigation costs should go down with more transparency.

We add all those costs up and put them all in the same chart and find out that there is an optimum amount of disclosure for each enterprise. We need to find a point where the total cost is the lowest to find the optimal disclosure. For this particular enterprise, $30,000 is optimal. If they disclosed more than that, then the competitive cost would dominate. If they disclose less than that, the information risk premium would dominate.

Think about what this enterprise will look like as we go out into the future. I drew that curve out over the next 12-15 years under some assumptions. That's the same top curve there, plotted one year after the other as we go into the future for about 12 years. It turns out that the key that tells us whether there is going to be more or less disclosure is what happens to the ability of the company's competitors to make use of the company's disclosures. If companies learn faster and faster to use this information, there will be less disclosure and total costs for capital will be higher. But on the other hand, if competitors don't take more advantage of this, then I predict that total cost will go down and companies will disclose more. My guess is that the second picture is the one that will be borne out. I think that competitors know much more information about enterprises than they let on today.

I therefore predict that capital costs will go down and disclosure levels will go up as we move into the future. One of the reasons for that is that disclosure really pays off. For a long time, I thought that this must be true, but there wasn't much documentary evidence of it. Last year, a professor in the United States studied hundreds and hundreds of public companies, and compared their cost of capital to the amount of disclosure that they give. What she found out is that those companies that are most transparent, that provide the most disclosure, enjoyed a 9.7 percent capital cost advantage over those that were less forthcoming. This 9.7 percent is a huge difference. Suppose you had one company that had to pay 10 percent a year to rent its capital and another had to pay 19.7 percent? What a huge disadvantage that would be?

This type of documentary evidence leads me to predict more and more public disclosure for companies. It is a balance point. On one hand, the company has a legitimate need for privacy from its competitors. But on the other hand, it has an obligation to inform its investors. It has to look for the compromise point is between transparency and opaqueness.

We can think about disclosure policy like this. If we were standard setters and figuring out what should be in generally accepted accounting principles, we could say on the vertical dimension we can look to something we're going to disclose. How informative is it to our competitors? And on the horizontal dimension, how informative is it to our shareholders and our creditors? Here are some examples of things that fall in each of those four cells.

In the lower left cell, something that doesn't give good information to anybody, either competitors or investors, would be something that we accountants really like a lot, historical cost depreciation. Nobody needs it for anything is as best we can figure out.

In the upper left hand corner is information that would be of no value to shareholders, but would be tremendously valuable to competitors. As an example, the secret formula for Coca-Cola. I show that in red because we certainly wouldn't want to ask Coca-Cola to disclose that. It's not beneficial.

But in the lower right-hand corner are things that would be very informative to investors but wouldn't really tell competitors all that much, i.e., things like high quality segment information by line of business and geography. These I code in green because they are good candidates for inclusion in a generally-accepted-accounting-principles model. They inform the people that we want to inform and they don't inform those that we don't want to inform.

In the upper right are things that are informative to everybody, and I have a question mark there. It would depend on relative costs and benefits. For example, a forecast of the sales for a new product just coming to market would be very informative to both competitors and investors. It's just a way to think about what you would put into a generally-accepted-accounting-principles model.

Let me wind up by telling you where I think that leaves us in terms of accounting. I pulled a definition of accounting out of one of the popular dictionaries used in this country. It defines accounting as, A system of recording and summarizing business and financial transactions in books, and analyzing, verifying, and reporting the results. That's how it's defined in the dictionary. I would assert though that in thinking into the future we need a different and broader definition. I propose this one: The information infrastructure necessary for an organization to achieve its objectives.

I want to point out two things about that definition. One is that it does not define accounting by the activities that go into it, like keeping books and analyzing records. Instead, accounting is defined in terms of the outcomes, which is the achievement of objectives. The second thing is that we're in an environment where accounting systems don't necessarily have to be thought of as totally internal to the firm or organization. With electronic connections to other firms in the outside world, one could think of the accounting infrastructure as being interfirm or interorganizational. It can take advantage of the World Wide Web.

If you define accounting as I have, it provides lots of opportunities to create types of value for decision makers many more than if you define accounting as a set of procedures necessary to produce a set of financial statements. And of course, if you define accounting as I have, an accountant is a person who enables an entity to achieve its objectives through the strategic use of information or information systems. I think that's a better way to think about what an accountant is and how accountants can add more value to enterprises and governments of all types in the future.

That summarizes my remarks. I basically started in the past, when accounting created a lot of value. In the present, I see these megatrends coming which are going to provide some threats to us as accountants but also open up tremendous opportunities. If we do the right thing in the future, in the 21st century, we as financial accountants and managers can create much more value than we have in the past. But it involves making some hard decisions now and moving in the directions that I have predicted.

That completes my presentation. Do you have any questions?

MR. DESTA (Ethiopia): I would like to thank you for your impressive presentation. What do you think about the main tenet of accounting in the 21st century, particularly regarding the generally accepted accounting principles? How are we going to change them? They will be the basis for the auditing profession as well. What's your opinion on that?

MR. ELLIOTT: The question about where generally accepted accounting principles will go and where standard setting goes is an interesting one. The International Accounting Standards Committee (IASC) has been working very hard to develop comprehensive, high quality standards that can be used around the world. I think that's a very favorable development. Of course, one of the reasons for doing this is lots of companies would like access to the United States capital markets. And so a very important consideration is whether the Securities and Exchange Commission in the United States will recognize IASC standards. They've said there are three conditions for that. The first is that they be comprehensive, second, high quality, and third, that they be rigorously applied. We don't know yet where that is going to go.

In my opinion, both the FASB in the United States and other standard setters and the IASC are asking and answering the wrong question. They are taking the model which I have just characterized as obsolete and extending it around the world. If I'm right, then a couple things are at issue. One is that that model is not descriptive of modern enterprises, and nothing that the IASC or the national standard setters are currently doing seems to respond to that deficiency. So I suggest that the standard setters are not facing the real problems.

The second thing I would say is this. The work that standard setters do is, to a large extent, centered on the formatting of statements, these balance sheets and income statements, and the disclosures that go with them. To the extent that the world gets electronically connected, those statements go away. We no longer need these general purpose, one-size-fits-all statements, because individual users will specify what they want, and they will obtain and format it for themselves.

You may be thinking that no individuals would be willing or able to learn all the protocols to do their own work. I suggest to you that agencies will grow up in the marketplace that will do that work for them. There will be technology-enabled vendors in the marketplace that will represent your particular point of view and provide you the information that you need. When that happens, there will be less and less need for the types of standards that are produced by IASC, the FASB, and other national standard setters.

Does that mean that there is no role for those standard setters? I think there still is a role, but that role shifts into a different mode. We need to define the minimum set of information that enterprises must collect for comparison across enterprises. To make it comparable, we will need common data definitions. When I report sales and you report sales, and an investor is comparing them, he or she should have reasonable expectations that we mean the same thing. Common data definitions and minimum information to be collected. I think standards will be needed in areas like that.

From what I've seen, it seems somewhat unlikely to me that any of the standard-setting bodies is going to migrate into that function. I see the possibility that standard setters themselves will become obsolete and a new form of standard setters might grow up, perhaps under the international standards organization or the UN. That's an excessively lengthy answer, but I hope I responded to your question.

MR. ENTHOVEN (United States): In the first part of your talk, you referred to the current financial statement, which is historically oriented and which is, of course, transaction oriented. You referred to the need to reflect more current values and also to value the state of human resources. That requires, I assume, a reorientation in the thinking of what the financial statements should reflect. I think this is very important because we don't reflect human resources nor current values. My second question is: Since there are a number of outstanding academics here, what sort of advice do you have for the academic world? What should we focus on if your model, which is a value-based model, has relevance?

MR. ELLIOTT: Let me address those two in order. The first had to do with the valuation of intangible assets, including human resources. I think I said, and I will reinforce the point, that I'm not suggesting that we value these intangible assets with a monetary value and put them on the balance sheet. The enterprise doesn't own the human assets. What I'm suggesting is that information about those intangible assets should be acquired and displayed in some form. It would involve a different set of measurements and numbers. It might yield measurements about the motivational level of employees, their morale, their educational attainments, their turnover on the job, or retention figures. It might be a different set of indicators that permits investors and creditors and other decision makers to find out whether the work force is becoming more loyal or less loyal, more productive or less productive. That I think would not lend itself to being described in dollars or lira or pounds or pesos. I see it not as an additional value put on the balance sheet with a journal entry, but as collateral information types.

Then the job of standard setters, if they choose to go in this direction, would be to determine the types of measures that could be used to disclose those things and what format and so forth. Or, if you go into the future world that I described, it would fit into the idea of the minimum information set and data definitions, so that when you evaluate employee morale, there is a common definition in all evaluations. I would not advocate reducing these things to accounting entries on the balance sheet.

The second question had to do with advice to academics because there are number of them in the audience. I'm not an academic myself, so my advice is free but probably worth what it's costing. I can't speak for the rest of the world. I can only speak for the United States where I observe it a little more closely. I would say that academics, to a large extent, are themselves trapped in this obsolete model. They are studying how to improve and put more bells and whistles on what I have characterized as an obsolete model. In the United States, that's the way to tenure and promotion and recognition, so I have little expectation that it's going to change because of anything I happen to say. Nevertheless, since you asked the question, I will answer it by saying that I think those professors, those academics who have already earned their academic stripes, who have gotten tenure, prestige, and recognition, might want to address a more normative type of inquiry where they actually thought about the emergent world.

I just gave you one scenario about the future. You could think about multiple scenarios, and you could think of the drivers of those scenarios and see what the common elements are, and where you might do research in order to provide the fundamental underpinnings of a new model. The balanced scorecard or that corporate dashboard that I showed you earlier has no theory to it. It's just a set of ad hoc responses to a situation where people are just not satisfied with what they're getting out of traditional accounting systems. It's a set of band-aids or first aid on a broken accounting model. I would suggest that highly motivated and intelligent academics might want to figure out what would be a better, more descriptive, more intellectually defensible model to describe future enterprises.

DR. DITTENHOFER (United States): I have a comment rather than a question. The Institute of Internal Auditors about nine months ago set up a task force to review the audit standards that had been issued by the Institute in 1978. The task force is using much the same methodology that you have been talking about this afternoon, the concept of megatrends and the impact of technological changes on internal auditing. We expect this to be presented to the Board of Directors of the Institute some time in December. When you say that academics have to change their method of thinking, I, being one, had to change my method of thinking to agree with the individuals on the task force. What we're doing is precisely what you have been talking about.

MR. ELLIOTT: We will all look forward to that. I think it might have big implications for all of us. I appreciate you saying that and I appreciate your attention.

A Financial Management Capability Framework for the Future

Hugh McRoberts, Office of the Auditor General of Canada

Thank you. Good morning. I'd like to say first how really pleased I am to be here, ladies and gentlemen, to have a chance to talk to you about the model that our team has been building over the last two years. It's now coming together. We have an exposure draft out and we anticipate publishing the model early in the next year. Now that it is really taking shape, we're pretty excited about it.

In my presentation this morning, I thought I'd talk a little about the project background, as well as a few words about a working definition of financial management, which was something we found we had to do before we could build the model. We'll talk about the model and I'll explain some of its architecture to you. Then finally, I'll come back to our diagnosis of some of the things in financial management, at least within the Canadian Federal Government, that have to change, and how our model has been designed to help change.

Why this study? The study is the culmination of a long-standing concern that the Office of the Auditor General has had about financial management. Really, our concerns began in the mid-1970s, when Jim MacDonnel came to Ottawa as the Auditor General and launched the first set of studies on financial management. Those had a fair impact on the Federal government, at least in terms of frightening it. We reported pretty widespread deficiencies in fundamental financial management areas. The government said, Yes, you were right, and promised to be good and did a few token things.

In the mid-1980s we did another study of financial management and found pretty much the same things were wrong. There were improvements in all of the areas, but the same basic issues kept coming up. By the 1990s we had the same sense that those issues were there and things weren't really moving. Also, we were getting some fairly basic questions.

As we looked across the financial management problems that auditors found every year, we felt a growing need to be able to put them into context. When you look at them, you can get one of two interpretations. You can look at the observations on financial management weaknesses and say, Okay, the government of Canada is a pretty big place. We do a lot of things. Some mistakes are going to be made. That's the normal cost of doing business in a well regulated, well-run organization. Or equally, you could look at them and say, These are the symptoms of a deeply troubled system. In discussions, both within our own office and with Treasury Board officials, we concluded that it was not entirely clear which conclusion was right. We really didn't have enough knowledge, overall, about the capabilities of our organization for financial management. So, that was a second motivation. We wanted to see if we could develop a tool that would allow us to assess. What is the overall capability for financial management in government departments and agencies?

When we looked around to see whether or not we could find tools to address those concerns, we found the various tools that were then currently available weren't really meeting our needs. A lot of them were very private sector in orientation, developed by the firms, to meet the needs of their private sector clients. But they really didn't reflect the realities of financial management in a government environment. They included issues with which government managers never deal and left out important issues that government managers really find central.

A lot of the others were long checklists, self assessment checklists which were good. They seemed thorough enough, but the problem we found is that once you were done with them, you had the answers to 200 questions, yes, no, yes, yes, no, no, yes. After that it wasn't really clear what the answers told you when you tried to sum them up, or indeed what you should do with the answers once you had them. Looking at it, increasingly, we felt that a more systematic or more organized approach to financial management was really needed. Financial management, good financial management, wasn't something that just happened in a vault. It was something that had to be designed and built. That's where we started.

The first objective, and one that became important from initial discussions we had with financial managers around the Federal government, was to develop a common understanding of what we meant by financial management. A lot of the discussions in the past have been crowded by the fact that at a very high level we all had a sort of general fuzzy notion about what we meant by financial management. This allowed us to achieve a lot of very high level stratospheric agreement without really actually knowing what we were talking about in specific terms.

So we set out to develop a clear, specific definition of what financial management was and what the boundaries of the activity were, so that when we engaged in conversation with people, we'd all talk about the same thing. We wanted a basis for implementing and institutionalizing the elements of financial management and financial management change. We wanted something that would provide a systematic and orderly way for organizations to move ahead where they had to; and to meet our own needs as an office, we wanted a framework for assessing financial management and financial management capability.

Before we started to build the model, we felt it was important to establish certain underlying principles, both for the model and for our office's approach to financial management. First amongst those was that financial management is not an end in itself. Financial management exists to assist organizations to achieve their objectives and to discharge their accountability obligations. It's not something that we want to set up as a shiny thing on a pedestal all by its lonesome. Secondly, financial management is a management responsibility, and that is something we felt was very important to stress.

As auditors, we have sometimes had a sense that management has simply said, Oh, well, that's the auditors' things. They'll come along and tell us what to do. Well, we're not going to. We want to lay the responsibility on management to determine the optimal level of financial management capability they need, to assess the risks and the challenges facing their organization, and then, to assess what they have to achieve to maintain that level of capability within their organization. This has some other implications.

Not all organizations are the same. Not every organization requires the same degree of capability and sophistication. Again, financial management is a cost activity. It doesn't generate revenues. It generates cost. So it's going to be cost-effective. You don't want $10 solutions for $2 problems. That also means that financial management has to be purpose-built and designed for each organization. There isn't a one-size-fits-all solution. You can't just put out a manual on financial management and say, Every organization from the Department of National Defense down to the Patent Medicine Review Board have to have everything all the same.

In terms of a working definition, we have decided and defined financial management as involving three elements: risk management and control, information, which is really the core of financial management, very intimately linked to all of these, and finally, the management of resources. Risk management and control involve two elements. One is setting in place the organizational structure and support framework that provides the environment for good financial management, e.g. executive support, a framework of ethics and values, and a risk management and control framework. This is an environment in which management has assessed its risks and has put in place appropriate controls to manage those risks.

Information is really the core of financial management. It obviously involves systems management, the development of the financial information, and ultimately the ability to link to non-financial information. This is one of the really critical differences in our view between private sector and public sector financial management. Put simply, if you look at both private sector and government financial statements, they look pretty much the same, but they reflect very different cycles of activities. In the private sector, you spend money so that you can get more back as a result of your expenditures. In government, the reverse happens. You extort money from the population so that you can spend it. You spend that money so that you can do something. The real management challenge is the linkage at the operational level between the spending and the doing something and optimizing that linkage. If your information doesn't include that non-financial information that links to your cost structures, it becomes very difficult to really engage in management and optimizing your use of resources.

The third element is management of resources. We've encapsulated the activities of strategic planning analysis, decision support, results in quality management, and resource and process management within the organization. In terms of decision support, the key here is the ability for organizations to understand before decisions are made what the financial consequences of those decisions are likely to be. Again, information is the core of this.

The objectives of financial management then are: first, to serve accountability; to report on the stewardship of public resources; to provide support for decision making; to support and assist in the generation of appropriate financial and non-financial information, both for decision making and for accountability; to provide the basis for the efficient and effective and economical use of resources; and to assist the organization in the management of risk, both financial and non-financial, through the establishment of an appropriate control environment with appropriate compliance with authorities. In the Federal government, and in most governments, expenditures from the public purse have to be done properly and only as authorized by the government. That's a very important part of government financial management.

The model we decided to adopt is a variation on the software capability maturity model that was designed by the Software Engineering Institute at Carnegie Mellon University. This model was initially designed at the behest of the U.S. Department of Defense, which in the 1980s became increasingly concerned with the fact that most automated systems didn't get delivered on time or within budget. Sometimes they didn't get delivered at all, notwithstanding the expenditure of a lot of money.

The Institute began to look at the organizational characteristics of software creators and began to evolve a model that said, Based on the organization's characteristics, we can predict the capability of this organization to take on a project, and on a reliable basis, deliver on complex tasks. The model has at its core some very good and generic organizational sociology. It was that core that we decided to adapt to our needs as a framework for the development of a financial management capability model. So, that's how we got started.

What is a financial management capability model? It allows us to describe the key elements required for effective financial management at a number of different levels of capability. It describes a potential evolutionary path or paths for an organization to follow in developing effective financial management. When we talk about a path, we're talking about a general direction. The particular path that any given organization will follow in applying the model is relatively unique. And finally, this is a tool for assessing the capability of organizations to deliver financial management.

The basic structure of the model is focused around assessing organizations in terms of where they sit on a five-level scale. Level I is the start-up level. Every organization has to start there. Some organizations never escape. Level II is what we have called the basic control level. At this point, an organization has established basic financial control; it can report its transactions and meet its basic stewardship obligations. Level III is the information level. In many ways, this is a transitional level. At this level, an organization begins to grapple with the issues of information, e.g., integration of information, linking between financial and operational information. At Level IV, having developed the information, it begins to develop the ability to use that information to refine it and to use it to manage and control its environment. It starts to move toward the achievement of specific goals and benchmarks. Finally, Level V is an organization that is able to seek to optimize itself. It has the information. It has the organizational structures, and it can become, in essence, a learning organization.

For each capability level, we have identified a series of key process areas. Each of those key process areas in turn has associated with it a set of goals. Each of those goals then is associated with a set of practices or activities. In assessing an organization, we look at practices, at the degree to which those practices then give assurance that the goals are being met. We ultimately assess whether or not the organization has achieved mastery in the key process area. That's the basic structure of the model.

In assessing a key process area, we look at a series of common features. For those of you who are familiar with the Institute of Chartered Accountants, COCO model, this will be a very familiar diagram. We have found that these represent appropriate key features that are part of looking at whether an organization has established mastery. In addition to looking at the specific activities and practices, we have to look at how they are imbedded in the organizational environment.

In terms of commitment to reform, we're looking at the actions the organization must take to ensure that the process is established with full management support. Is there an ethical system in place?

In addition to having the procedures established, do they have the right people? Are these people supported, trained, appropriately managed?

Are activities well structured? Are they well organized? Is anyone assessing how well these activities are doing from a management perspective? Are there standards there which allow management to assess the degree to which the activities are happening in the way in which they expect them to happen?

Is there external verification to provide management with an objective assessment about the way things are evolving?

Those are the sort of basic common feature elements that are looked at in assessing each of the key process areas. Now what I'm going to do is to walk through the model. I'll describe very briefly the capabilities associated with each level. You'll have a quick look at some of the key process areas. When we get to Level II, I'm also going to take one key process area, what we call stewardship reporting, and just take a couple minutes to drill down into that area to talk about the process area, the associated goals, and some of the associated practices to give you a flavor of the details of the model. I couldn't give you the whole thing. The model has a document about that thick. I thought it would be useful for this audience to have a little bit of flavor.

Level I is an organization, often a start-up, but it's really an organization that hasn't reached Level II. It doesn't mean it doesn't have capabilities, but its capabilities are not well developed and they're not uniformly developed. They're probably not articulated well. The organization is usually operating in what I call emergency mode. Organizations can get stuck there. Through heroic effort, often at the expenditure of large amounts of overtime and often the health of its employees, the organization will continue to get by and occasionally even generate a success. But, the organization never manages to find the time or the energy to get the traction necessary to really make its processes and procedures repeatable.

When we look at a Level II organization, we're looking at an organization which has managed to establish the capabilities to develop realistic financial plans, and to manage and control its resources and allocate them toward the achievement of plan objectives. It can produce accurate and reliable data within decision-making materiality. It has the ability to report, for stewardship purposes and accountability purposes, on what's happened.

The key process areas, and we've organized them under the three broad features of our financial management definition, include: establishing a basic control environment for risk management and control; establishing the basic level of management support for this activity; establishing a set of ethics and values that everybody shares and works from; and establishing basic internal controls. Information is focused on data management, establishing basic general accounting; getting the general ledger up and running; and providing good operational data capture and the ability to meet stewardship reporting. Under management of resources, there is planning, budgeting, funding and getting basic operational control over expenditures.

One of the key process areas mentioned was stewardship reporting. The purpose of stewardship reporting is to meet legislative reporting requirements and support decision making by legislators by accounting for the use of resources, and producing timely, operational financial reports to account for their use. So, it's supporting both external accountability and basic internal management. We've got cash flow control here.

The stewardship reports comply with the requirements that Central Agency needs. The reports are complete, accurate and timely. Timely is particularly important, as well as the capability to generate analytical and ad hoc reports.

To do this, we have activities or practices including: clearly defining the reporting requirements; communicating requirements and deadlines to those responsible for doing it; assigning responsibility for preparing reports; monitoring the status of the production process; assuring that the activities amongst the various players who must pull this thing together are coordinated; reviewing the reports for compliance with the requirements; and approving those reports before submission for accountability.

Common features important for stewardship reporting include: senior management sponsorship and involvement; established policies and guidelines; adequacy of resources; assignment of responsibility, authority and accountability for the reporting; a link to resources; effective senior management review and oversight; and independent assurance by senior management before information is sent forward.

Moving on to Level III, one of the features of the model is that is additive. When you move from Level II to Level III, you don't start over again. Level II is a foundation to which you add to get to Level III. Level III then represents the foundation that you add to, to get to Level IV, and so on.

In terms of the capabilities, here the organization begins to develop the capability to integrate operational systems and data; to anticipate and manage risks; to develop reliable information for management; and to staff with the necessary skills. All of these are important, but the one that is really critical at Level III, and is almost its defining element, is the ability to move from general financial information to integrated information. Information is generated in a way that is meaningful to the operators and which allows them then to match that information with the information they are gathering on the results of their activities and on their outputs. At this point, you're starting to get operational cost data generated.

In terms of the key process areas, financial management skills development is very important. If an organization is going to progress from Level III to the higher levels of capability, it has to start paying attention to the skills of its personnel and ensure that those personnel have the necessary training and development opportunities to enable them to meet the challenges of establishing these capabilities. Intergroup coordination becomes increasingly important. At Level III, financial management can no longer be a stove-piped element. It can't just be the bean counters over in the corner doing their thing. It now has to start reaching out to the organization and supplying it with information it needs and also understanding what the organization's financial management needs are.

Financial management systems have to becoming increasingly integrated and linked with other organizational reporting and operational systems. Management information and reporting becomes increasingly important. In Level II, the focus is on stewardship reporting. In Level III, the focus is on information for management.

Increasingly, now, we're starting to look at performance measurement, quality measurement, cost management and resource management, Level IV key process areas. Information management, organizational performance information become increasingly important. At this point, the organization is beginning to develop the capability to really look at itself in a hard way to establish benchmarks for its performance and to monitor progress against those benchmarks. At Level III, the organization was basically saying, How are we doing? At Level IV, the organization is saying, How well can we do? There is a big difference in the thinking that lies behind these questions.

Finally, moving to Level V, the key capability here is the ability to continuously improve the organization's financial performance. Here the organization has really developed the capability to transform its historical information into meaningful and reliable perspective information, both financial and performance-related. In terms of management of resources, it is establishing strategic improvement targets and has a very, very heavy emphasis on quality improvement. I guess the example here would be organizations like Motorola. You're no longer looking at an organization that is benchmarking against itself, against past performance. You're looking at an organization that is saying, We are establishing the benchmarks now in terms of best of breed, and we have the capabilities to assess how we're doing against them. That can be a real stretch for many organizations.

When we started all of this, we had some thoughts on what needed to change, how the world had to evolve, and the best model to meet these changes. The first one is the need to move from stovepipe systems to integrated systems. Organizations can no longer afford to have half a dozen different systems which exist in their own particular stovepipes, very often suiting only their owners rather than those for whom they were developed, and neither talking nor linking to each other. We've got to move across the page to integrated systems.

The systems don't have to be all one big system. That can often be a mistake. But part of their design and engineering within an organization has to be the ability for one system to generate information in frames that are relevant for the other systems.

We have to move from a data orientation to an information orientation. Data are still critical. They are the basis for information. The emphasis increasingly must be not on data that becomes an end in and of themselves, but rather as a basis for the creation of information. From bookkeeping to financial management, we've got to get rid of the bean counter image.

We are moving away from a pure control focus to a focus on financial performance, from a historical perspective to a future-oriented perspective. We don't have to abandon all of our old activities. We simply have to change the emphasis. We still have to have some control. We still need bookkeeping. We still need historical financial information. But we have to realize in each of those instances that they are no longer the end.

And, finally and most fundamentally, we have to move from a focus that says that financial management is the responsibility of financial managers to a view that says financial management is the responsibility of everyone in the organization.

What does the model provide? We believe it provides first and foremost a communication vehicle, the basis on which we can now engage in discussion with management in the government community. It is no longer ambiguous as to what is meant by financial management, what is its domain, what is its scope, what are the expectations. It is a framework for assessment, the basis on which we and management can assess what financial management capabilities are present and which ones aren't. We believe that ultimately this model will be more important for management than for us. We believe it will give managers in government a tool that will allow them to think in a systematic way about what financial management capabilities they need, and about what their risks are and are not. It will give them a tool that will allow them to identify the gaps that exist between what they need and what they currently have, and will provide them, finally, with a road map to close those gaps where they believe it matters to do so. It's a road map for orderly change. It also provides off ramps.

For organizations that have relatively unchallenging economic or financial environments, some of the levels are stopping points. Level II can be a stopping point for a relatively small organization. Perhaps equally important, the levels provide rest stops along the way for organizations that have longer roads to travel. Moving from Level I to Level II provides a point at which an organization can stop, pause, and perhaps engage in some congratulations that there has been a concrete level of achievement. When it moves to Level III, again, it's a point to pause, to reflect, and to celebrate.

This ends my presentation. Thank you for your attention.

MS. ROBINSON (United States): I was intrigued when you started talking about your model and the purpose of this tool, that is to assess the capability of an organization to perform financial management. I noticed that your organization has audit responsibilities and financial management responsibilities. I'd like to know what kind of receptivity you're getting from your users, your audience out there, on using this model. Do they use it themselves or do they ask you to come in and see how it works first?

MR. McROBERTS: I don't have any past tense answers for you. What I can tell you is that so far the reception has been good. We've just had the exposure draft out for a couple of weeks, but timing is perhaps fortunate for us because our model is coming out in the context of something else. I welcome your question because it gives me a chance to talk about it.

About the same time as we started on our model, the Treasury Board, which is basically the central agency responsible for financial management in the government, began a process of looking at controllership in the Federal government. They established a blue ribbon panel under the leadership of the head of the Canadian Comprehensive Auditor Foundation. He and a number of distinguished leaders from the Canadian business community spent about nine months studying controllership and, about this time last year, published their report on the modernization of controllership in the Government of Canada. That report has a very similar vision of the future to that envisaged by our model.

Over the last year, the Treasury Board has been developing a process to move that report forward within the Government of Canada. Recently, they have started asking organizations to assess their current state of controllership. At the same time, we have been meeting with the senior financial managers in a number of these organizations to give them our models. What we have now is an exposure draft, so we're meeting with these people and we're leaving the model with them saying, This is what we propose to use. This is the structure. This is going to be the basis on which we'll talk about financial management to you in the future. Before we finalize and publish it in January, give us your thoughts and comments. Are we talking about a world you recognize?

Those discussions so far have gone extremely well and a number of those managers have seen in our model a concrete way in which they can respond to Treasury Board's requirement to assess the controllership capability. Indeed, they have been asking us, Look, rather than you coming in and doing this to us, how would you feel if we did it to ourselves and then you can audit that process? We haven't given them an answer yet. One of the things we want to do is look a little more closely at self-assessment processes and make sure we're comfortable with what the self-assessment protocol would look like, what the information expectations would be, what documentation expectations we'd have of an agency. But I think it's a very fruitful way to go and it's one that we want to explore further, provided that at the same time we can establish a process that meets our needs and continues to preserve the independence of our office.

MS. PARRILLI (United States): You mentioned that you're looking at self-assessment models and protocols. The COCO model was developed in Canada, and I understand there are self-assessment workshops that have been devised in Canada to deliver this model. Do you have any experience or any thoughts on it?

MR. McROBERTS: Yes, we've looked at those models. The control self-assessment workshop approach can be a very good approach for certain purposes. However, in talking to managers that use it in their jurisdiction, they have suggested that its use as a basis for assessment is probably not entirely reliable. Internal auditors in organizations who have used it have said it's good as a diagnostic tool. It's very helpful to management as a management tool in identifying and dealing with non-financial management problems in their financial management shop. But from an audit point of view, they view it more as a scoping tool than an audit tool itself, which suggests to us that the evidential base may be a little bit weak. We are looking for something a little more structured and a little more document-based.

MR. PORTILLO (El Salvador): I'm sure all of us have encountered public employees who react indifferently to performance standards established for the tasks they are assigned. How do we motivate these employees to improve their performance?

MR. McROBERTS: This is certainly a very difficult problem. I think one of the difficulties that modern government organizations face is what might be called the decline of the value consensus. I think it is fair to say, and certainly there is some sociological evidence to support this, that in the 1940s and 1950s, perhaps as a result of the experiences in North America coming out of the Depression and the Second World War, that there was a fairly strong value consensus within the society. That value consensus began breaking down in the 1960s, even more so in the 1970s. One of the challenges organizations face is one of ensuring, within their organizations, a certain consistency of values amongst their people.

Of course, you cannot compel people to all have the same values. What you can do in an employment context is at least make the values that you expect clearly guide their activities. I think this is perhaps the most important step we can take. Organizations are spending time trying to clarify and articulate, in many cases for the first time, what values or ethics they want to guide their organization. What are the choices, what is the hierarchy? I'm not sure that's going to solve the problem, but about all I can say at this point is that it's a start.

MR. HUGHES (United States): As you were explaining the five levels, I was reminded of the ratings given in white water rafting where Level I is very easy and smooth and Level V is very, very rough waters. It seems to me that this is a very similar situation. I was also reminded in Italy, they have a system of ratios that local governments send to their central government so that the local governments can be evaluated as to their financial management capability, their degree of solvency. At some point in time will this system require the provinces to send in ratios to assess their financial management capability?

MR. McROBERTS: In our structure, in theory, it would be possible. In practice, it would be suicide for any Federal government to even think the thought. Provinces view themselves virtually as coequal states within the confederation. I think if the Federal government suggested that it was going to require these sovereign entities to provide it with proof of their financial management capability, it would be in very serious political hot water immediately. At the same time, we are aware that many of the provinces are interested for their own purposes in assessing their financial management capabilities. The Province of Alberta, although it has not taken the type of road we've taken, has been very aggressive in the last few years in assessing and challenging its capabilities in these areas.

MS. ROBINSON (United States): I think it is a wonderful system you've outlined. As an educator, what are the ways and means and the respective vehicles you're using to train or retrain your respective people? This must be a tremendous task. I just wonder what systematic way or unsystematic way you carry this out.

MR. McROBERTS: You certainly touched on one of the challenges that we have. The first challenge we have, in fact, as we start to roll the model out, is going to be training our own people in the office. Fortunately in our office we have an excellent professional development group who are giving us great support on this. In fact, next Tuesday, I am going back to a meeting with our professional development people to start outlining the basic syllabus for a senior management orientation program on the model for our office.

The next challenge we have is training the auditors to apply it. Then, from there, the challenge really moves to the Federal government, under the leadership of our Treasury Board, who are going to have to train in the context of not only our model, but in the context of their controllership modernization initiative, and in the context of our financial information system modernization initiative that is also going on in Canada.

We are in the process of revamping entirely the basis on which financial information is gathered and managed in the Federal government. This has to be pretty much in place by the Year 2000 because for many entities this is their response to the Y2K problem as well. It also includes, in addition to a technical fix, a completion of the move from a cash-based basis of accounting to full accrual accounting. That is also going to pose enormous challenges for the current workforce and the need to train and upgrade that current workforce to move from a transaction-based type of processing that is really cash-based to an accrual-based accounting. They need to rethink the way in which they handle transactions, both physically and conceptually, in carrying out these accounting functions. You have indeed put your finger on a major problem and a major challenge that the Federal government of Canada is going to have to face over the next four or five years.

50 Years Progress of the U.S. Joint Financial Management Program: Much More To Do!

Karen Cleary Alderman, Executive Director
Joint Financial Management Improvement Program, USA

It's a real pleasure to be here with you today. I'd like to thank Virginia for that very kind introduction. She mentioned that I have followed in her footsteps. I feel like the new kid on the block trying to talk about the history of JFMIP, where Virginia made more of the history than I have, I assure you. She can tell me if I've got it right.

What I'd like to share with you this morning is a snapshot of things that we are doing in JFMIP: where we are focusing in the context of the history of the program; what we're doing right now to support the Chief Financial Officers' (CFO) systems strategy; what we're trying to do with program management offices in leveraging information technology to support Federal government agencies; and also some efforts on human resource development.

What is JFMIP? Joint Financial Management Improvement Program. It's a one-of-a-kind type of operation. I frankly had no appreciation of its full context and flavor when I took the job. As I commented to Virginia, I have grown to admire her ability to walk the tightrope. This is a joint undertaking sponsored by the Department of Treasury, the Office of Management and Budget, the General Accounting Office and the Office of Personnel Management, working together in program agencies in the executive branch to improve financial management policies and practices. I can guarantee you that these various agencies don't always view the financial management objectives and systems with exactly the same lens. There are variations in that lens.

The JFMIP serves as a catalyst for action. We mobilize resources. We coordinate efforts to accomplish specific objectives that are laid before us by the steering committee. Basically, it is a consensus building organization.

JFMIP was initiated in 1948 and actually institutionalized in legislation in 1950 through the Budget and Accounting Procedures Act. In terms of major changes over time, I think the next major milestone was 1966 when the Civil Service Commission, which is now our Office of Personnel Management, joined JFMIP in a leadership position in the human resources area financial management human resources development. The effort at that time was to improve recruiting, training and job classification. I would have to say those challenges are as fresh today as they were in 1966.

A major change in the responsibilities of the JFMIP occurred in 1996. That was with the passage of the Federal Financial Management Improvement Act. This is part of many legislative actions that have occurred in this decade focused on improving Federal financial management. This particular law requires agency heads, not the CFOs of agencies, to substantially comply with three things. They have to comply with Federal accounting standards that are issued by the Federal Accounting Standards Advisory Board. They have to comply with standard general ledger at the transaction level. They also have to comply with financial system requirements that are issued by the JFMIP.

How are we organized? I belong to many different organizations. The leadership comes from the principals, which are the Director of the Office of Management and Budget, the Director of the Office of Personnel Management, the Comptroller General, who heads the General Accounting Office, and the Secretary of the Treasury Department. My actual management comes from a steering committee which is at the CFO level or the director of management level in government. It is like the number three position in government. JFMIP sits under that. I have a very small staff which is leveraged with volunteers and liaison activities that come from the Federal agencies. In addition, a small permanent staff is being established. I'll tell you how it's funded, which is an interesting story in and of itself. It is a permanent investment in systems requirements, developments, testing and certification for the Federal government. So JFMIP is a central agency to do those types of activities.

JFMIP over time has had many different roles, and I don't know all the roles. In part, we respond to the direction of our steering committee to issues that are relevant at different times. In the last decade, the JFMIP has been a key partner to the CFO Council's systems subcommittee.

In 1990, the CFO Act was passed, which among other things established the CFO Council consisting of CFOs from the largest 24 Federal agencies in government. That council works on problems that cut across government. But prior to 1990, there was no institutional setting other than organizations like JFMIP to work cross-organizational issues. It was the Office of Management and Budget who had that role to some extent, but the Office of Management and Budget also had the budget role. So there was a bit of an adversarial relationship between the agencies and the Office of Management and Budget when discussing how many resources you had and there was a difference of opinion.

The CFO Council institutionalized a collaborative role for the CFOs. They meet monthly. Under the CFO Council, there are about seven to eight committees; the number varies depending on what issues are being managed. The systems committee is the committee that deals with the financial information technology architecture issues for the Federal government. Its principal role is defining the financial system functional requirements, not the job of the chief information officer, but the functional requirements that financial systems have to perform to meet government internal stewardship and external reporting requirements.

The CFO Committee has adopted a strategic plan and that plan has a variety of parts. Part of that plan has to do with systems strategy, and the key strategies are to standardize information, so that data means the same thing across the Federal Government; use electronic data interchange, which is a shorthand statement that means you enter data once and you pass it electronically; and use commercially provided software and commercial transaction processing services to the maximum extent possible. Basically, there was a decision or a consensus starting back in the mid-1990s that the Federal government no longer had the resources to be the developer of financial systems. There was a very robust commercial market out there that could provide us these capabilities at lower cost and better value than we could do for ourselves.

The nominee for the OMB Deputy for Management and currently the Office of Management and Budget controller, gave a very interesting talk about a year ago. It encapsulated the Federal government's strategy for financial software systems, and that is: to build partnerships with private sector providers; provide market information that encourages private sector partners to furnish products to us, the Federal government; to make it easy for qualified vendors to get on the GSA schedule so that the customers, the Federal agencies, can procure financial systems without lengthy delays; to maintain up-to-date financial standards, and that means up-to-date financial systems requirements statements; reengineer procurement vehicles so that they are easy to use, flexible and provide a wide selection of products; and then provide incentives that encourage private sector companies to update products on their nickel. We should provide them enough market information so that they have incentives to compete with each other to provide superior products that meet our needs. That is a summary of the strategy to engage the private sector market.

Virginia knows this egg very well. Some people have labeled it the wheel of fortune. Basically it is a description of the system requirements for financial management. At the core is the core financial system, or the core accounting system. Around it is managerial cost accounting, which is the set of protocols to break down costs against products so that you have cost per output information. Then, outside of that are the 13 or so principal subsidiary systems or feeder systems into core financial accounting. These would include, in the Federal government arena, budget formulation, revenue, acquisition, property management, inventory, grants management, insurance claims, benefit payment, direct loan, guaranteed loan, seized and forfeited assets, and there are two general administrative systems, the travel system and the personnel and payroll system. That architecture defines the scope of Federal financial activities. Most of the subsidiary systems, except for the two administrative systems, are program areas that are mixed system areas. They have a financial component and they have a program management component. Then, outside of the subsidiary systems are the departmental executive information system and workstation support tools such as data warehouses.

The job of the JFMIP system is to define, through a collaborative process, the minimum standard functional requirements that must be met internal to Federal government and also must be met by potential providers of software from outside the government. It is an articulation of the functions that must be met in government. It's a way to organize the markets. Think about that egg. That egg started to be populated back in the late 1980s with the definition of the core requirements for basic accounting, the center of it, and worked its way out. Then, think about how information technology systems have been developed, at least in our government. I bet this model is similar in your own government.

We call this the Nots, Gots, Cots, Services Transformation. Nots is not off-the-shelf. That is where we were in the 1960s. The United States Federal Government was a leader in developing, for their time, extremely sophisticated information technology, mainframe systems to manage very large complicated processes. In the Department of Defense we had very large mainframe systems to pay all our military and civilian personnel. The Social Security administration developed large integrated mainframe systems to process transactions associated with Social Security, and similar systems were developed by the Office of Personnel Management. But these were one of a kind systems developed by government employees with the support of contractors. They typically were not transferable because they had a lot of agency-specific characteristics. The concept of defining standard minimum requirements was developed in part to allow for a government off-the-shelf process to be developed. If HEW or Health and Human Services developed a travel system, perhaps it could be transferred over to another agency. So we were defining common government specifications, but over time we found that these high level statements of requirements also generated a market for commercial providers of software and services to meet these requirements. People found they worked.

Some of the early areas had to do with travel. The travel requirements attracted a couple of commercial providers who in time have really improved their products so that you can really do desktop travel arrangements. All estimated travel costs can be obligated in advance. After travel, you update your voucher based on the earlier entry of data, and you have it all in the desktop from the authorizing official approving it through the transfer of data to the accounting system. These types of packages were generated by commercial providers in response to some of the early high order functional requirement statements. Of course, you have to come to consensus about what your functional requirements are, and do some reengineering of your business practices or consider common business practices.

Then, we move across the specter from using commercial services to support governmental financial practices to using third party transaction processing. How many of you use a travel card provided by a commercial vendor, like AMEX or VISA, provided to you by your government? This area is one of the biggest revolutions occurring right now in the Federal government financial systems for transaction processing. Back in the mid-1990s, when I started in Department of Defense travel practices, there were about 200,000 of our 2.2 million military and civilian personnel who had been issued travel charge cards. For the rest, we used cash advances and there was a lot of cost associated with that. When I left, in 1998, there were about one million personnel who had been issued charge cards. That became the standard business practice. Department of Defense personnel could not get a cash advance unless there was no other way to meet the mission. That new business practice in travel has been institutionalized.

Small purchases is the next area of use for commercial charge cards. In the mid-1990s, less than $1 billion of total transactions under $2,500 in the Federal government were procured using a purchase card. Again, that may be a Visa, MasterCard or other card with central billing capabilities. This year, $7.7 billion in transactions were done through the purchase card. These are buying goods and services for the Federal government, or supplies through commercial providers or perhaps through electronic mail or pre-negotiated contracts. So rather than processing a purchase order, you just use commercial transaction processing services. The cost per transaction is much reduced. Moreover, you capture information on commercial platforms and pass it back into our accounting systems after reconciliation.

In the area of electronic benefits transfer, we are using a debit card infrastructure to provide food stamps and other types of welfare payments. So the Federal government is moving more and more into using commercial infrastructure where we are a small percentage of the transactions and also we don't pay the full cost of the infrastructure.

In terms of major trends in financial management technology, moving from in-house or not-off-the-shelf developed products to commercially developed products and processes has been accompanied by tremendous change in the technology base. Back when I came into the government, back in the old days, we didn't have desktop computers. We used Selectric typewriters and did lots of cut and paste. A special team had control of the mainframe computers. You would put your request in and then you would get a printout back a week later or whenever they got it into the queue. In the 1980s there was some dial-in and other facilities to make the information a little more accessible. But in the 1990s, the technology base changed again dramatically to distributed systems where you're using a client server that has online reporting and a different ability to combine data. Also, there is the World Wide Web. How many of you have children who have grown up in the computer age? What does a mouse mean to them? Does it mean a little rodent, or does it mean a little machine that clicks? What do webs mean to them? That your house needs cleaning? Or does it mean this Internet from which we pull information?

The technology base that Federal financial managers are dealing with has changed dramatically and is going to continue to change dramatically. It's causing tremendous stress on the system and tremendous stress on our workforce because they can't keep up with the changes in technology. Nevertheless, how that becomes more important for us is to get down to basics and ask, What are the needed functional capabilities? What do the Federal financial managers need? Then, let this tremendously vital industry come up with a whole variety of different ways to get at the answers. This government's strategy has been to define what we need and let industry define how to provide those needs.

What is the current financial systems environment in the U.S. Federal Government? Basically for the 24 CFO agencies, the major Federal agencies, there are 811 financial systems out there. There are 1,100 applications. We spend about $1.6 billion a year maintaining all this stuff. About three-quarters of those applications or agencies report that they have a useful life of five years or less. Only about ten percent of those systems are commercial, off-the-shelf. A lot of those commercial, off-the-shelf applications are highly customized. The two areas where we have a lot of commercial, off-the-shelf systems are areas where we made an effort to organize and market, and that's core accounting and travel systems. That's going to change over time. There is a vital commercial market for our personnel and payroll systems. The agencies report that 60 percent are ready for upgrade or replacement in the next five years.

I want to talk a little bit about the status of the JFMIP requirements. Consensus building for what the basic requirements are is a hard job. I've learned that because I have to update and reissue these documents. Basically, when I took over in January, the areas for which there had been a common statement of requirements included only guaranteed loans, direct loans, seized and forfeited assets, the travel system and the personnel and payroll system, the inventory system, core financial, and sitting on my desk ready for a launching, was the managerial cost accounting system requirements. Also sitting on my desk was the General Accounting Office's effort to break these system requirements down into audit guides that were going to be used by the audit community to check compliance.

Remember I mentioned the Federal Financial Management Improvement Act required agencies' heads to certify substantial compliance with the JFMIP system requirements. I looked at these and found that some of these documents were produced ten years ago, hadn't been changed since, while the laws and regulations had changed. In some cases, entire regulations like the Federal Personnel Manual, which was frequently referenced in one document, had been abolished. In other words, I became very concerned that agency heads were going to be asked to substantially comply with systems requirements that had been created for a different purpose, no longer the right one.

So, what we did was undertake updating initiatives for all but inventory and managerial cost accounting documents, which were just issued. We have different working groups. We call them affinity groups. They are led by a principal agency. For travel, the General Services Administration leads. For personnel/payroll, we are working with teams led by the Office of Personnel Management and the key payroll agencies to update these system requirements, streamline them, and refine them. That is underway now.

We looked at those functional areas that had never been developed and said, Where is the pressure coming to get a standard statement of requirements to meet a major government area? In the grants area, the Federal government transfers a lot of money to States and a lot of money to universities to do various functions, e.g. research, support for different functions. We had about 16 or 17 different grant systems and the States were going nuts because in some cases they had to deal with 16 or 17 different processes to do basically the same financial function. When States in our system get fed up enough with having to deal with too many different processes, they start taking the political route to enact legislation for the Federal government to clean up their act. That's where we are on grants. The CFO grants management community and the program organizations that deal with grants have come to the agreement that they are going to formulate a grant systems requirements statement.

Another area is property systems. The Federal government can’t pass their consolidated financial audit because property systems, property accounting, are not in a state with which they can get a clean opinion. There is no standard statement of property system requirements. We are going to ask an external organization to help bring the various agencies together to help develop a statement of property system requirements. Again, that may stimulate a commercial market, but we’re hoping that this sort of reduces the amount of variation across Federal agencies and brings a consensus of what systems have to do in those areas.

In the JFMIP Program Management Office, in addition to updating and maintaining and communicating requirements, we are streamlining the process by which the government agencies procure core financial systems. One of the things that agencies had to do was buy systems that had been certified through a test that the software met Federal government agency requirements. However, the testing process was part of the procurement process, and in our government that meant that nobody was allowed to have any information, either agencies or vendors, about the nature, the details, or the results of the test. Therefore, agencies were retesting everything before they procured a system.

What we are doing now is separating the procurement process from the testing and certification process. We are defining requirements more specifically to requirement source, that source being legislation, a regulation, etc. We are going to separately develop a test and a certification process. That will be done under JFMIP. Then we’re going to post all the details about the requirements, the test scenarios, the results of testing, up on an electronic repository. We call it a knowledge base that is going to be posted on the Web, and everybody the agencies, the vendors, anybody else can see what the requirements are, how they are being tested, and what the results are. We will test the mandatory requirements. In addition we’re going to collect information on value-added features that are of interest to agencies. We feel that this process will help organize the market and help standardize expectations in the Federal government. We have had too many secret processes that only get us in trouble.

Basically, the JFMIP Program Management Office’s role is going to be to develop the requirements, communicate with stakeholders, educate, develop and maintain those tests, maintain a knowledge base and act as a clearinghouse. That’s what we’re going to do. We’re going to use the Web. The Web is low-cost information-sharing methodology.

I’ve talked about systems requirements. I will talk about human resources development. In addition to those two principal portfolio areas, we have also done ad hoc initiatives.

Virginia mentioned the Travel Reform and Savings Act. Basically, I don’t know how your Federal governments work, but in ours, we have a process. When legislation passes, it becomes part of the mound, and then other things are layered on top of it, and other things are layered on top of that.

Then, the agency has to deal with this mound of requirements. It sometimes becomes a constraint to intelligent behavior, or common sense behavior.

The Travel Reform and Savings Act was an effort to allow for modern business practices in travel, but we had to clear off some of the underbrush. Some of the underbrush was things like the 1939 Telephone Act that said that every long distance telephone call had to be certified by a supervisor. In 1939, long distance telephone calls were probably something very different. In 1999, it costs more to certify each call than the call itself, under commercial practices. Virginia acted as a catalyst to get consensus on a legislative package to eliminate legislative barriers to modern, efficient business practices in government travel, and sold it to Congress, and it is now implemented through the various agencies.

The Single Audit Act was another example of collaborative action by JFMIP. In grants, which involved a lot of different stakeholders and parts of government, everybody was getting into the act in terms of auditing. The same grants were being audited at a variety of levels. The Single Audit Act provided legislation to allow for a single audit to cover all these different areas.

Now I want to talk about human resources. I mentioned that there is this technology explosion. There is a major transition in the way we meet certain functions, i.e., relying on commercial software and commercial transaction processing. At the same time, our government has been going through a process of downsizing, and focused on administrative support areas to downsize, which includes financial management. Financial management has been targeted as an overhead function that needs downsizing. At the same time, we have had an explosion of legislative mandates in the financial management area. I mentioned the Chief Financial Officers Act. There are others such as the Government Management Reform Act and the Government Performance and Results Act that basically say to Federal agencies, We want dramatic changes in some of your basic business processes. We want you to have strategic plans, performance plans, performance reporting, and we want you to be able to pass financial audits. We want you to do a whole variety of things that you haven't done before. At the same time, you're facing a technology revolution, and by the way, downsize. Okay? Moreover, we will penalize you if you fail. Or, We'll give you report cards. A lot of Federal agencies got Fs on those report cards.

JFMIP has been working, and Virginia actually provided a major leadership role in this effort, in partnership with the CFO Council and Human Resources Committee to help build some tools to help financial managers describe and define the competencies that are necessary to survive in this new environment. Those building blocks are the core competency documents that have been produced by the JFMIP in concert with key players in the Federal agencies who deal with these functions. So we have produced statements of core competencies. What do the financial managers in the Federal arena have to know?

In addition, we are working with information technologies and vendors to identify offerings that teach and train on those core competencies. We're trying to use Web technology and search engine tools to allow agencies and individuals to quickly find the course offerings that provide training to meet core competency areas. The idea, again, is to provide a framework for folks to find what information they need, and take action on it.

Sharing information is another role of the JFMIP. We put on an annual conference in March and we have publications, quarterly newsletters, all of which we put up on the Web under FinanceNet. FinanceNet is the Web page of the Federal financial managers. Also there are continuing activities, including an annual national award program which recognizes the best of breed in financial management for large and small Federal agencies and State governments.

In summary, JFMIP does serve as a vehicle for management improvements. The focus areas, currently, are systems, technology and human resources. We do it all at the behest of our steering committee.

Our Web page address is http://www.financenet.gov/jfmip/jfmip.htm. You can find lots more information there. We have a very short time for questions.

MR. MALDONADO (United States): I am from Barents Group. Briefly, you did not address directly the issue of the Year 2000 problem. Is the Joint Financial Management Improvement Program playing a role in it? If so, what is the status? Can you give us an idea of what the cost of the program is going to be for the Federal government at the financial management level?

MS. ALDERMAN: Other than stating in our systems requirements that they have to be Year 2000 compliant, we are not in charge of the Year 2000 issue. To address the Year 2000 problem, there is a special office associated with the White House, headed by John Koskinen, who was formerly the Director for Management at the Office of Management and Budget. He is heading the Year 2000 project for the Federal government and also the broader partnership with industry to assess where agencies are with respect to having systems that are Year 2000 compliant. They have to have remediation plans.

In terms of cost, I can't tell you the cost for financial systems, but I think by the end of FY 1999 the Federal agencies will have to spend close to $10 billion to remediate Year 2000 deficits in all of their systems.

MR. ALVARADO (Honduras): Dr. Lozada explained in his presentation that competition is a problem for public administration because public officers only have the attributes that the law gives them and they cannot go any further. You're saying that here in the United States many public agencies or Federal agencies use a credit card to purchase goods locally. How free are they, how far can they go in these offices in making these purchases? As far as I'm concerned, it scares me to know a public officer can have a credit card without any limit on it.

MS. ALDERMAN: Credit cards can be set up with hierarchies and profiles which include rules that the credit card company imposes at the behest of the sponsoring agency. These can be set in terms of who can use it, total dollar for a single purchase and total sales that can go through a single card, and that can be specified by month. You can also put commercial screens into these cards that block certain types of purchases. On the travel card, only travel type services can be purchased. Purchases outside of the travel industry can be blocked. There are commercial company mechanisms that can put all sorts of controls at the transaction level. In addition, there is management information that comes back that says exactly what was purchased and who holds the card.

In our government, the card is becoming the standard method to purchase goods and services costing $2,500 or less, the micro-purchase threshold established in law. However, the Federal government is looking to use these cards even for intergovernmental transactions, or purchases between government agencies. We're going to create a methodology using the debit card type of transaction, where there is a transaction fee per transaction. This will allow the General Services

Administration to sell supplies to any other Federal agency using the card transaction processing capability to capture the information and pass the information back and forth to accounting systems. Our government is committed to using the commercial structures to the maximum extent possible. Moreover, you collect data centrally through commercial processes that you can interrogate a lot easier than reconciling all those paper records.

MS. ROBINSON (United States): Karen has tremendous responsibilities in the accounting and financial management area, but there are two other groups of professionals who have a lot to say about the limits on credit cards. Sometimes they have a lot more to say than we'd like to hear. The audit community weighs in heavily on the controls that have to be established for the use of the cards. They also have something to say about the policies that Karen develops. Then there is the procurement profession. They weigh in heavily too on the parameters established for the use of the cards. There are lots of people looking over the shoulders of the users to make sure they are complying with all of the government requirements and limits.

MR. EINHORN (United States): You have big shoes to fill, but you'll do it. I think JFMIP should have more active contacts with universities, at least in the Washington, D.C. area We tried that once at the American University where I was teaching, and the only problem I had was they constantly referred to JFMIP as JMIP. I know it's early in your time, but do you have any thoughts about the educational institutions becoming familiar with JFMIP? It's a great source.

MS. ALDERMAN: That's one of my favorite topics. I'm very interested in engaging the universities in our area as well as other universities more broadly to offer not just exchanges of information but opportunities for internships at the Joint Financial Management Improvement Program. I have also worked with other training programs like the Women's Executive Leadership Program. Since I've come on, we've had five Women's Executive Leadership Program folks come through the office for their 30- to 60-day developmental assignments. We let them swim with everybody to help carry on the functions. If anybody has any ideas on how to better establish these opportunities, please give me a call. I am absolutely interested in exchanges of ideas and also offering internship opportunities. We have a lot to learn from our young folks, particularly on information technology, and they have a lot to learn and opportunities to do so at JFMIP.

MR. HAMILTON (United States): Karen, thank you for such a comprehensive presentation. I know Virginia and some of the others who have been with this program for a long time understand it very well, but for some of the rest of us, this was a very nice profile of the history and the comprehensiveness of the program.

I'd like to put a plug in for a sister organization on the same network, FinanceNet. I'm sure if Preston Rich were here, he'd probably say some of the same things. I was playing around on FinanceNet a week or two ago because I was getting ready to give a presentation to 18 Ukrainian businessmen and women at the Commerce Department. I focused on the resources available on FinanceNet. It's truly impressive. Some of you may know that all the Chief Financial Officers of the U.S. Government, as well as Canada, Australia and a growing number of nations around the world, are easily accessible on FinanceNet. It's a great resource.

MS. ALDERMAN: For very small organizations that are trying to reach a large audience, FinanceNet and Web technology, combined with new tools like search engines, will make all of our jobs a lot easier. That's a strategy we intend to employ. Thank you.

Record Systems for Accountability: A Strategy for the Next 20 Years

Piers Cain, Director of Research and Development
The International Records Management Trust, London

I'd like to thank the conference organizers for inviting me to speak. It is very unusual for anybody in my field to get the opportunity to talk to financial managers.

Public financial management constitutes one of the most fundamental responsibilities of any government. In an era of economic policy reform, it has become the critical element determining the overall ability of any government to manage the economy and to ensure transparent, accountable government. Moreover, it is now widely recognized that corruption diverts resources from poverty elimination. Improvements in the management of government finance are essential if the global escalation of corruption is to be halted.

We need to reinforce the drive toward accountable government. Accountable government is a much broader concern than purely financial accounting, but accounting is very important in this process. Underpinning accountability initiatives is the assumption that the evidence of official actions and activities exists to be audited, and these can serve as a measure to monitor accountability. Records provide a reliable, legally verifiable source of evidence of decisions and actions, and thus responsibility. They are a powerful tool in constraining individuals from engaging in corruption. Thus, accountability must be supported by sound, reliable, authentic and accessible documents or records. This is in many ways a statement of the obvious, but I think it's something that needs to be restated from time to time. Let's look at the relationship between records and financial management.

This table illustrates the relationship between records management, accounting and external auditing. On one layer, you have records management, which manages records through their life cycle, starting with creation of the record. There is an active phase when they are being used in people's offices, and then a semi-active or inactive phase when they are used only occasionally. Some records will be active for a week or two and then be stored somewhere else. Other records are used in your office for much longer. Of course, you need some financial records only until the records are audited, in other words for perhaps seven or eight years. Other records you must keep much longer. An example would be personnel records, which obviously you need to keep right through to the period of retirement for pension purposes. Records may be kept for permanent use or destroyed. About 98 percent of records are destroyed eventually. About 2 percent can't be destroyed, perhaps for historical reasons.

Above that layer, you have typical accounting functions: budget and planning, internal audit and control, financial management and reporting, and the integrity environment. Above that, you have external auditing: attestation, performance appraisal, quality assurance, certification and reporting. The point, of course, is there are three layers and each has to be in place if you're going to have an effective system of accountability.

It is the record keeping that gives the form and substance to financial systems. It provides the means by which financial decisions and transactions may be verified and reported. For every function in financial management, there should be a financial system and records being produced by that system. You have processes like planning, assignment and financing leading to budget and then budget records.

In practice, the records management layer is often missing in government financial control systems. This can be a significant factor in some weaknesses. Without the evidence-base, systems will continue to deteriorate. Accountants and auditors, of course, do understand that records need to be kept for accountability. But often they and senior public officials do not acknowledge the need for records *management*. In other words, the need to manage those records over time.

Now, more often than not, records keeping is seen as purely a clerical function requiring low intellectual ability. This would be true if only the rudimentary filing aspects were considered. However, record keeping in a modern bureaucracy is a management function. It is not simply limited to keeping individual documents in a filing system.

It is important to understand that the records management function encompasses managing control over the entire life cycle of a record from its creation to its final disposition. This involves obtaining both physical and intellectual control of the records created throughout an organization including aspects such as identifying, capturing, maintaining, preserving, accessing and disposing of records when their value to the organization ceases, or transferring them to an archive facility if they are determined to have long term administrative or historical value.

Moreover, as administrations increasingly implement computerized systems, record keeping is becoming a technically more complex area. Although the fundamental principles of keeping records in an electronic environment are more or less the same as in the paper environment, the skills required to manage them are very different. The importance of maintaining the links between electronic and paper record systems is critical if you're going to have a complete picture. Typically the traditional filing clerk does not have the skills to do this. At the same time, this is not an area to which information technology (IT) systems designers have given much thought. Programmers and IT support staff are concerned with current systems and preparing for the next generation of systems. Records professionals need to develop and implement strategies to deal with a broader scope of legacy systems as well as current systems and future implementations to ensure that the valuable evidence of transactions and decisions is maintained over time. I emphasize this issue of maintaining over time. The traditional electronic financial system was designed to provide information for the period prior to audit. If you start creating electronic government and electronic record keeping, then you need to keep those records for much longer periods, and that's where you run into problems.

If a system of financial management breaks down, we know the consequences are serious. Typical symptoms would include: inadequate systems for monitoring and lack of information, including financial information; the inability to produce accounts on time, which of course renders them of limited value for expenditure control and monitoring; the failure to keep votes ledgers properly, which, of course, is an important tool in expenditure control; and weak and limited auditing capabilities. The causes of these symptoms may be multiple, but they are often related to problems in the management of records. Yet, people rarely make the link between problems in financial management and inadequacies in the way records are managed.

Rather than describe this myself, I'd like now to show a video clip. This video clip is a documentary set in The Gambia, where the Commissions of Inquiry was set up to investigate the abuse of government finance. This is really a short case study. The point of showing the video is a kind of reality check. We've been talking about these very advanced systems that are being introduced in the United States and elsewhere. But for many countries, that isn't the reality. I thought it would be quite useful just to see the contrast between different kinds of reality.

(The following is taken from the video.) The thefts which actually disenfranchised the people of The Gambia covered the whole spectrum of public sector finance. For about 10 years, the auditor general did not present audited accounts to Parliament although that was a mandatory requirement of the Constitution. For ten years, the president was aware, the Parliament was aware, but did nothing about it. The lack of record keeping was deliberate. There were procedures in place, but people in management were more interested in overriding controls for their own purposes. In a country as poor as The Gambia, in some cases, 80 percent more was spent on the president's travel than on education for the whole year. The expenditures for the president's household was about 60 percent more than expenditures on drugs and dressings for the whole year for the whole country. The expenditure on foreign travels was more than health and education combined for the whole year for the whole country. So you have a situation where the little revenue that comes in through customs, through internal revenue, taxation, is dissipated through foreign travel. The investigation teams uncovered the documentary trail of economic crime through sheer determination to work through the mountain of available financial records.

In the long term, it must be the chain of accountability established by the Constitution that safeguards government assets. Within this chain you have different players: the audit office, the minister of finance, the judiciary, the public, the media. For the auditors, the lynchpin of the whole system, the disorganized state of records is a major deterrent to achieving their mandate. What it is all about is promoting and holding public accountability. We have to review financial systems, and now with the mandate to conduct performance audits, we have to review all management practices and this is where the documentary evidence comes in. Without it, the audit really cannot proceed. It is exactly what this office right now is experiencing. Every time we embark upon an audit, we find that the auditee has not kept good records. Our job is to audit. It's your responsibility to put the proper filing system in place so that we can access these records. Do what is necessary for keeping these records. If auditing is deemed to be the cornerstone of good government, which has everything to do with accountability, then we will not move ahead.

In fact, the necessary mechanisms are in place to address the problem. The government of The Gambia's Civil Service Reform Program is one of the first in Africa to incorporate a records management component. The National Records Service Act of 1993 provides a sound base for control of official records. However, despite major improvements, work on financial records management systems is still at an early stage. The National Records Service ought to work in partnership with the Accounting Records Department to ensure that a more effective system is put in place for the management of accounting records. The Federal share regulations provide for the maintenance of various accounting records. But they are not properly kept. Accounting personnel need to know how they should be kept, where they should be stored and how they should be maintained. If we have a system in place, we can set our standards. I see the need for a great number of courses to be run designed specifically at sensitizing people on the need for adequate record keeping and the impact that it has on overall accountability.

Despite difficulties with intermittent power supplies, lack of trained computer personnel, problems with accurate source data, and vulnerability to hackers, The Gambia is steadily computerizing its financial information systems. Undoubtedly, many of the loopholes in financial control will be closed.

There will be significant efficiency gains, but the integrity and security of the documentary evidence, which has been the basis for the return to democracy will have to be protected if accountability is to be safeguarded. The National Records Service will have to cater to electronic records. We have been able to computerize the company section. We are working very seriously to computerize the government section. You have to set the system in the its proper perspective before we are in the position to do away with our manual system.

Computerization has not reduced the number of manual records we keep. We still need physical records as evidence of transactions. We have the new problem of storing computer tapes. At the moment, we're storing tape in the computer room itself. We should find a location separate from the computer room to store tapes. The opportunities for better use of government information are increasing tremendously. The information unsupported by authentic and accessible documentation is unreliable and useless.

I'm sorry we missed a bit of the video, but I think there is enough there to give you an impression of what we intended.

Computerizing government, of course, adds to the problems that any government has in keeping its records. The requirements for ensuring that electronic records support good government and accountability are only now beginning to be articulated and understood. Professionals in those developed countries where computer applications have multiplied rapidly over the last decade are fast realizing the enormity of the issues involved. We can look to the United States where your National Archives has been sued several times over record keeping issues in the electronic records area. We can look at other countries as well. Already there are chronic problems in reading, retrieving, decoding and accessing electronic records over time. There are a growing number of instances of gaps in the evidence required for accountability.

Probably the leading countries who have done work on this are the United States, Canada and Australia. There are other parts of the world such as Germany that have also done work on this. Australia has one of the most advanced electronic records management programs in the world. Yet, an inquiry by the Australian Law Reform Commission uncovered a state in many government departments with no guarantees that the older paper records had been preserved or that new electronic records had been kept. In fact, the commission president said in the *Sydney Morning Herald*, Our review found mediocre and fragmented record keeping is so widespread within the Federal administration that its failures are not accepted with a degree of fatalism. The inquiry report expressed concern over the rapid adoption of electronic records, such as e-mail. A high proportion of the Commonwealth of Australia records are now generated electronically. The president of the commission went on to say, Yet the record keeping system to which it (a record) belongs, is often no more than a server filled with an unstructured mass of records which are difficult to locate and are subject to intermittent purges. What I want to emphasize here is that this isn't just a problem that can occur in countries such as The Gambia, which is disadvantaged in many ways. This is also an issue for industrialized countries.

Governments create and use financial records within a regulatory, institutional and functional environment. The national constitution often requires regular reporting to the national legislative assembly. Finance and audit laws generally require ministries and departments to ensure that financial and accounting records are kept and managed, and empower auditors to obtain access to all financial records. No surprise there. Accounting instructions and financial regulations promulgated under these laws set down more detailed requirements for accounting and financial records. Yet, there is widespread noncompliance with these requirements for financial record keeping.

The lack of structure and systems for controlling financial records, and the lack of accountability for their management are major contributing factors in noncompliance. Most countries have legislation that defines official or public records and establishes national archives responsible for overseeing implementation of its provisions. Typically it will require that records of permanent value are, at the appropriate time, transferred to a place of deposit (usually public archives) where records are made available for public inspection under certain conditions and safeguards. Of course, legislation should specify the destruction of records that are no longer required for administrative or historical purposes. This destruction must be carried out in an authorized and controlled environment, and a record of the destruction maintained. If you can just simply go around destroying records without any record of what you're doing, that in itself is a great way of covering up wrongdoing.

As for the issue of fraud and corruption, inadequacies in managing records can also contribute to a climate where fraud and corruption flourish, as we saw on the video. In particular, certain kinds of fraud are carried out through the concealment of records or through false recording. Corruption and fraud thrive in the absence of transparency and accountability. Many efforts to encourage accountability are thus turning their focus to combating corruption as a way forward.

Public sector corruption is commonly interpreted as the abuse of public office for private gain. This little equation I'm quoting is from a man named Robert Klitgaard. Most often it occurs where there is a monopolistic situation, M, involving a wide area of discretion, D, and low or no capacity to enforce accountability, A, for actions taken. As you can see, this relationship is expressed as $C = M + D - A$. Within this scenario, it is widely accepted that corruption is characterized by activities of a financial or commercial nature resulting in enormous profits or benefits. It is often only detected on paper or more recently in electronic systems, and is easily hidden through loss, theft, destruction or concealment of records. It allows proceeds to be concealed and/or disposed of without detection, and sometimes beyond the jurisdiction where the crimes were initiated.

Most corruption and fraud occur where the public and private sectors interact with one another. Situations where a member of the private sector requires a provision of a service, or the application of specific regulations or levies that are controlled by the public sector, are particularly vulnerable to corruption. For example, a member of the public meets a civil servant face to face at a counter to obtain a vehicle license. The public official can either give you the license or make it difficult for you to obtain it.

In many countries, reform measures are being developed and tested to strengthen certain institutions and improve financial controls. The objective is to limit incentives for civil servants to participate in corrupt and fraudulent behavior. These should include strategies for well-managed records because investigators need to access organized records to assemble them together to reveal inconsistencies that can pinpoint and lead them to the source of corruption.

The way records are controlled throughout their life cycle and the responsibility for this activity are also key issues. Monopolies over the availability of public records and data provide opportunity to extort bribes. Information may be sold or the records themselves may be removed from the system to conceal some kind of wrongdoing. As a result, strong management is needed to control the records and limit the opportunities for tampering, loss or destruction of the documentary evidence of official transactions.

If financial management systems remain weak, and the ability to hold public servants accountable for their decisions and actions is obstructed, corruption will flourish. Records management can be a preventive, verifiable and cost-effective restraint when compared to prosecution. It's obviously much better to prevent fraud happening in the first place than to try and get the money out of the wrongdoer later on.

If corrupt officials know that there is a paper trail, or perhaps an electronic audit trail that can be audited, they are less likely to engage in corrupt activities. Conversely, a clear paper trail can protect the innocent from false accusations. In fact, in the case of The Gambia, there are officials that were protected from prosecution because they were able to show through the records that they were actually innocent. Sometimes it's not just a question of prosecuting the guilty. It's also protecting the innocent. In the case of The Gambia, where it was tied to a military coup, it was quite a serious issue to be accused by the authorities of corruption.

Let's think a little bit about an agenda for the future. Records management is a specialized management function. It imposes control on records systems while still enabling the monitoring and comparison of records documenting different transactions. That's obviously critical if you're looking at fraud. Until public officials and senior civil servants recognize this function as a management issue, it will not be possible to enforce compliance with record keeping requirements and establish the necessary culture for creating, maintaining and using records.

I want to go through a list of things that could be done to progress forward. First of all, it's absolutely critical to develop and maintain a culture for creating and using records. In some countries where the oral tradition is very strong, such as parts of Africa or Indonesia, this is a real issue. For example, in Indonesia, the minister of a cabinet actually set up a program to help develop a language for recording government activities because Indonesian is rather a flowery language, and speakers were somewhat ambiguous in their statements. His effort was also intended to encourage better record keeping so that there was a means of tracking what decisions had been made. So, in other words, we really need to identify the demand side for information and to look at how records are being used and what they want from those records, and how realistic it is to meet those needs.

We need to strengthen to role of records management and records managers within an institution. This needs to be totally integrated with the introduction of information technology. It requires auditors, IT specialists, accountants and records people to work together. It is certainly not an issue that records managers can work on alone.

We need to look at records legislation. This is to ensure equity and fairness of government operations and to protect citizens' rights. In countries where there is no Freedom of Information legislation, which includes the United Kingdom, I think we will see in the next few years increasing pressure to introduce these kinds of reforms.

We also need to look at standards. There are in fact standards emerging for records management programs. Probably the most interesting standard is being developed in Australia. It is called AS4390. It will probably provide the basis for a global standard. Even at this stage it represents a substantial endorsement for the need to determine responsibilities governing the capture, maintenance, access and disposal of records that satisfy record keeping requirements in both paper and electronic environments.

Considerable work is underway on records management issues in North America, Europe and Australia, where corporate memories of organizations are increasingly held electronically. However, this work is highly theoretical and difficult to apply. When we turn to governments in developing countries, often they do not have access to this research, certainly not in a form that is useful to them. I think part of the agenda must be to empower developing countries.

There is some value also in just looking at standards for paper-based documents, but I think in the future it is going to be a less useful thing to do. There are perhaps more needs for standards for electronic record systems. One issue is the standards for formatting data. These should be determined by a range of factors, including cost-effectiveness, immediacy, usability, importance, practicality, popularity, conflict with existing standards, and retrospective impact and compliance. Until recently, most information technologies did not contain records. They contained data, but not records. I think this point needs to be reiterated. Unlike information systems, record keeping systems contain materials which are, amongst other things, highly redundant. They almost inevitably are out of date. However, if you want to have a statement of what was done, or you need to be sure that somebody did something, you need a permanent record of that. It's time bound. In other words, it will have a date stamp on it. It must be inviolate. You shouldn't be able to change it without controls.

These of course are characteristics which information systems developers try to avoid, particularly with regard to redundancy. So there is a conflict between the need for record keeping and the efficiency of an information system.

I think other speakers have mentioned the potentially devastating effects of hardware and software incompatibility. Coupled with rapid obsolescence, this increases the need to rely on information technology standards to access records and data over time. The computer industry's seemingly frenzied objective of getting products into the market in an attempt to displace competitors has resulted in situations where, and I'm quoting here, ...the increasing complexity of most computer systems along with the mushrooming of different systems are creating such incoherence that in comparison, with the Tower of Babel would seem monolingual. In other words, we have a situation where there are so many different systems going on that it is difficult to keep things together.

System-specific technology dependence presents overwhelming obstacles, impeding the capability for data being migrated across time and across systems. So, this whole initiative toward open systems standards is critical, but I'm sure those who have been involved with it are aware that we have a long way to go in that area before we truly have open system standards that really work.

Notwithstanding the tremendous growth in automated systems, we should not ignore standards for the maintenance of paper records. In countries where paper files are going to remain the reality for the next few years, we could probably do with some standardizing. For example, in countries that use registry systems to manage paper files, the rotation of staff within or between registries should become a standard method of operation. This would reduce corruption opportunities by reducing the ability of an individual to establish monopoly and extort bribes.

Clearly, as we look to the future, we should be looking at ways of assessing the vulnerability of records systems to corruption and fraud. In many countries, although there may well be auditors' reports saying that the records that they need are not maintained properly and they cannot provide a true opinion, it's very rare for any public official to be disciplined for not keeping the records properly. That's where the auditors really have a role to play.

Finally, there is a role for records and records management in supporting accountability. If we're looking at the new and powerful electronic systems that we wish to introduce, we need to include the records component in all of this if we are going to have success. Thank you for your time and attention.

MR. HAMILTON (United States): One point you made which I thought was very interesting regarded the integration of manual record systems with computerized systems. Perhaps you could elaborate just a bit on some examples of how that's done. I'm looking at the year 2000 problem we're having, some of the audits I've done of the computer department at the IMF and other agencies have indicated that documentation of computer systems has been lacking. I wonder how much of the year 2000 problem we're experiencing could have been prevented if computer records were maintained properly so systems could have interpreted them.

MR. CAIN: You make a very good point about the often very poor state of systems documentation. I think it reflects a culture within the IT industry that is obviously not looking to the future. It's been a technology that's been developing extremely quickly. We're probably paying the price for that. I think it's also worth emphasizing that as we move toward putting more and more of our long-term records onto these systems, this is going to become much more important. Someone mentioned the number of systems within the U.S. system being replaced in the next few years. It was a very high number indeed.

It's going to be much more important when we need records for maybe 50 or 60 or 70 years rather than 10, to ensure that there is a pathway from one system to another. We can't lose important pieces of data along the way. One of the problems with migrating data is that it's often very difficult to capture all of it. So over time, with each migration, you tend to lose more and more detail. It's rather like using a photocopy and copying a copy. Eventually it starts to blur.

As to the integration of paper and electronic systems, we need to keep it simple because there is a real difference in the way computer systems and paper systems work. For example, in a personnel payroll system, you don't want to migrate it onto another system and give it a totally different number. As long as you keep that number, you can have that number assigned to the paper filing system. You could have it on every single sheet of paper that relates to that individual, so you can file all those things together. You can also look at things like directory systems that mirror your paper system. A key point here is simple linkages. I think that's the most important thing to do. Paper systems are difficult to change quickly. In a computerized system, if you decide that you want to replace the value of a field, you simply key it in and it can actually change a thousand or a million records all at once. With a paper system, somebody has to find that file, pull it out and write that new piece of information on the file. The key is to think very strategically, very simply.

MR. HAMILTON (United States): If I might add to that, I know for many, many years we could count on the U.S. General Accounting Office to issue reports on the lack of documentation, especially in the financial systems area. I haven't seen any recently. I know we have auditors in the audience and I'd like to reemphasize the point that Piers made earlier. It's going to be up to the auditors to emphasize the importance of records management when they're reviewing systems. A lot of the U.S. auditors now, especially in the Federal government, are devoted to reviewing the financial statements so they can provide opinions on consolidated financial statements. That's such a major task. I just don't recall seeing anything related to records management in those audit reports. It will be up to us in the financial management community to emphasize the importance of records management. If it's not brought to the attention of managers by the auditors, then those of us in the other part of the financial management community will have to do it.

Government Auditing: The Challenge of the Future

Moderator:
Kenneth Dye, President, Cowater, Inc., Former Auditor General of Canada

Panelists:
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Professor, Florida International University
I.P. Singh
Deputy Comptroller and Auditor General of India
Peter Armstrong
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Kenneth Dye, President, Cowater, Inc., Former Auditor General of Canada

Good afternoon everyone. This is a government auditing session, and we have three diverse presentations this afternoon. Mort Dittenhofer is going to lead off to discuss the reengineering of internal auditing. Mr. Singh is going to follow discussing developing country audit challenges. He'll be speaking mostly about his own country, India, and the SAI there. Peter Armstrong, from Canada, will wrap up with a two-pronged address: the first about audit changes in Latin American supreme audit institutions, and secondly a discussion about what is going on at the INTOSAI Development Initiative, IDI. After our speakers have presented their views, we will complete the session with a question period.

Before we start, I thought I'd just mention my generalized impressions based on some of the countries I've been working in with their SAIs. There is a common thread to many of the problems they experience. Most of their problems are rooted either in the mandate, which is usually outdated, or in the funding. There's a lack of appropriate funding to do the job they're mandated to do. We see quite a disparity in audit strength around the world and their ability to get the job done. Many of the developing country audit organizations could improve their audit methodologies, and there is lots of methodology around. It can be pretty-much borrowed from other places today.

The audit technologies are beginning to be strengthened. You do see computers now in supreme audit institutions, which you didn't before. I think the PC is going to be the saving grace. They won't have to go through all the nonsense that we went through in North America with our big mainframes. They'll be instantly into information technology.

There is a huge need for training. Training is not well structured, and usually not related to promotion or to the work the people are doing. There is lots of opportunity in the training side, and I know that Peter Armstrong has been doing some of that.

Financial auditing, which you would think would be the basis of many of the audit shops, is not terribly well done in many, because they haven't been focusing on financial auditing at all. The focus is often on compliance. As a consequence, there is a lot to be done in the financial audit world before they leap forward into value for money or performance auditing.

I think these weaknesses stem, as I said, from inadequate budgets. Also, salaries are not competitive with the private sector. As a consequence, you seldom see dynamic, qualified professional accountants in the audit shops. The big problem, I think, is that their Parliaments are not getting useful, timely audit reports from their SAIs. There are rare exceptions. We have one exception where leadership has made the difference, and that person is in the room today. Eric Harid from Zimbabwe has a remarkable, modern, supreme audit institution to which other African nations are now looking for help and leadership and training. Another organization that sort of transformed itself into an effective audit organization is from the little country of Bhutan. Not many of us get to go to Bhutan, but it is a charming country of great beauty. Their little audit shop is only 100 people, but they're dynamic. They know what they're doing, and they're auditing for the King there. So there are little pockets of excellence around the world in developing countries.

Let me introduce Dr. Mortimer Dittenhofer.

Dr. Mortimer A. Dittenhofer
Professor, Florida International University

The material I'm going to present to you this morning has been developed in part from some of the lecture material that we use at Florida International University. We are one of the IIA accredited programs in internal auditing. There are only 30 of them in the world, and we have one at Florida International University that we think is the best of the 30. I'm not sure they would all agree, but we have come up with many ideas on restructuring, reinventing, trying to make the internal auditing operation a more efficient type of operation. That's what I'm going to talk about this afternoon. To fully discuss the paper from which I'll speak would run about an hour and a half. They told me I only had 30 minutes. I'm going to be taking pieces from each of the sections. There are some 20 different sections in the paper. I'll just give you an idea of what is in these sections. The paper, which will be available after our session, will contain the full material. For those of you who are active in auditing, it may be of assistance to you. If you're not active in auditing, it is conceivable that some of your associates back home would be interested in getting some of these ideas as potential improvements that they could make in their auditing.

I'm going to start with a general statement, that the concept of change is inevitable, and hopefully change is for the better. Internal auditing is a relatively new discipline in both the public and private sectors. Its organization and its evolutionary progress have represented change not only in methods, but also in the philosophy of conducting the affairs of organizations in these two sectors. Probably one of the most important events in the evolutionary progression of internal auditing was the issuance, in 1972 by the U.S. Controller General, of audit standards for government, the Yellow Book. Those standards expanded the audit process into operational areas with the intent of measuring efficiency and effectiveness, in lieu of the time-honored objective of regularity and freedom from malfeasance, misfeasance and nonfeasance.

As was mentioned previously, today's auditing deals with improving efficiency and effectiveness, and yet rarely do we apply the technique of internal auditing to the internal auditing process itself.

How can we make this operation more efficient and more effective? This afternoon we're going to talk about this proposition. How can internal auditors do better with less? By better, we are going to consider a qualitative output and outcome through the use of reduced employment of resources. There are three areas, generally, that we'll be talking about, and the 20 different sections cover them: philosophical, methodological and operational.

The first area that I'm going to discuss is visions and missions. In the past, internal auditing organizations believed it essential that they have a charter. This document described such items as authority, responsibility, methods of operation, position in the organization and reporting structure. Current thinking is that this charter is not enough. Students of organizational operations find defects in it because it is too limiting and because it does not address the potential benefits of internal auditing that can be provided to all of its stakeholders.

It is now believed appropriate to establish a vision statement, a description of what the internal auditing organization will do and its contribution to the well-being of the parent organization and to those organizations and individuals associated on its periphery. The vision statement serves as an objective with a series of goals that will enhance their existence and service.

The mission statement is more concrete. It might be said that it's a description of how the vision will be accomplished. Missions are descriptions of activities to be accomplished by the internal audit organization. They have a specific intent and a definable impact in a specific and demonstrable area of activity.

Internal auditing organizations should go through these exercises in order to establish the big picture of why it is in existence and what, ideally, it should and will accomplish. With these pictures in place, the organization can develop congruent plans, policies and procedures.

The next area is customer service. A new development that has been recently emphasized in business and in other types of organizations is to consider service for the customer. In auditing, the customer can have several identities: operating management or the auditee, middle management, top management, the audit committee, the external auditor and government. In planning the audit schedule and in planning the conduct of the audit itself, this customer orientation should be considered.

The internal audit organization should be active in trying to determine what it can do to help these various classes of customers. It should be proactive in anticipating their needs, and in making plans to accommodate them. Some of these audit activities can be special projects within the expertise of the auditing organizations that will be responsive to these customers' activities and responsibilities and that will enhance their value and contribution to the organization as a whole.

The next area is quality control. The concept of quality permeates my entire presentation. Standards of quality must be observed and they will produce information that is dependable and appropriate for use by the audit department's customer. Many of the other sections of my presentation contain suggestions for auditing practices that will contribute to audit quality. Also, the reference to the Institute of Internal Auditors' Standards for the Professional Practice of Internal Auditing contains others that should be mentioned. A brief coverage of the standards provides these elements: that auditing should be performed with objectivity by auditors who are completely independent in actuality and appearance; audits should evidence the use of comprehensive planning and should show the considering of allowing for contingencies; the audit should reflect the application of appropriate skills, background and experience of the staff. There is a series of other provisions that add to the quality operation which is available in the paper.

The next area is working with audit committees. Several of the sections cover the relationship between the internal auditing organization and the audit committee of the board of directors. The internal auditing organization can and probably should serve the committee in a dual capacity first, as a service source for committee functions, and second, as a source of intelligence for management purposes. It can provide background information and training for the members of the committee, determine committee members' independence, and assist in committee oversight of financial and reporting activities. The internal auditing organization should be a provider of information for the audit committee. The internal audit operation can consider business risks, determine adequacy of internal controls and assure the validity of financial statements.

The next area is considering risk aspects. It has been conventional wisdom that auditing of various organizational functions such as purchasing, management of capital assets, cost distribution and motor pool operations, for example, can be performed on a cyclical basis. To a degree, risk and exposure were generally considered in establishing these cycles. However, the result was not what we needed. Many audits contained little in the way of substantive findings. Findings were of little interest to management other than to disclose that the audit had been performed and things generally were under control. Areas where there was risk and exposure were given little attention because the audit effort was diverted to the cyclical audit approach.

Management may have been aware of potential problems relating to financial risk, marketing risk, sensitivity risk and objective risk. However, the audits were not programmed to audit material risks in these areas, unless they were a part of the cyclical audit output. Thus, audits were not productive in response to the material aspects of these risks, and, thus, they were not providing management with information for use in the development of the strategic directions of the organization.

The factors of risk that generally are recommended include such things in the external area as technological development, changing customer needs and expectations, competition, new legislation, natural catastrophes and economic change. Internal factors that should be considered relative to risk include such things as information systems design, quality of personnel, changes in management responsibilities and the nature of the entity's activities. To these factors we might add several more common factors that are operational in nature, such as quality of internal control system, size of the entity in revenues and assets, the liquidity of assets, complexity of operations and situations where there has been rapid growth.

The next area is improved communications. Audit reporting is probably one of the most sensitive parts of the audit process. Regardless of the quality of the auditing examination and evaluation in the field, if the results are not clearly transmitted to management, the audit effort is of little value. Auditors are normally told to exhibit standard characteristics in their reporting, such as clarity, brevity, timeliness, completeness, freedom from jargon and acronyms and using positive language. There are several other items that should be considered. One is keeping in mind the needs of the recipient. The report should be responsive to management's needs and the report should be so tailored. The second is responding to the level of understanding of the report's recipients. The auditor should consider the recipient's background, education and position in the construction of the report. The third area is emphasizing quality aspects. The reporting should not only describe the activities that are being reported, but should also describe quality aspects so as to provide the reader with a complete picture of the situation.

The next section is a reduction of processing time. One of the frequent complaints of the auditing operation is the extended length of time it takes to process an audit report after the field work has been completed. The complaint used to be made of the periodic financial reports also, until new methodologies and electronic equipment provided for almost overnight production of financial and operational reports. Management wants to know promptly the results of the audit. Consequently, long delays associated with mathematical precision and legal reviews are not acceptable.

The flattening of the audit organization, which we'll talk about later, and the authorization of competent audit officials at lower levels to issue audit reports will provide some help in this regard. However, there are other steps that can be taken to reduce the delay in the issuance of the report or to provide important audit information promptly. Several of these steps include meeting with the auditee on a weekly basis to review current audit results, issuing informal interim reports to management on important audit findings and obtaining the auditee's position. If possible, write audit report drafts in the field concurrently with the audit work and obtain the auditee's comments at that time. Use word processing and other electronic equipment for the writing of the reports and the development of accompanying items such as charts, graphs and photo illustrations. There are several other items that you will find in the report relative to this subject.

Another area is auditee self-assessment. A technique of the auditing process that has been used by some audit organizations is the client self-assessment, or the client's self-audit. It is a simple arrangement whereby the audit staff outlines steps that it would normally conduct in the process of the audit. The outline contains what would be in the audit program including the objective of the testing, the method to be used, a sampling plan, the conduct of substantive testing, and the reporting as to the result of the testing.

The auditee, not the auditor, then performs these tests, arrives at a conclusion, and presumably takes corrective action where needed. The auditor reviews the work of the auditee and performs tests where it is believed necessary as a preliminary to accepting the auditee's work. This process is somewhat like the external auditor testing and accepting the work of the internal auditor during a regularly scheduled annual financial audit.

This methodology helps to reduce the audit time, provides early information to the auditee as to conditions found, and reduces the audit cost. However, it must be kept in mind that the internal auditor is responsible for the auditee's self-assessment. Thus the steps must be clearly defined and the testing of the auditee's work must be professionally performed following accepted audit procedures.

Another area is the use of new methodologies. Recent technical developments in computer activities have provided internal auditing with new sophisticated methods. One of the most dynamic areas of audit processing is the use of computer-assisted audit techniques. This methodology is not new, but continued improvements are being made that materially increase the efficiency of auditing accounts receivable, inventories, accounts payable and fixed asset accumulations. This methodology consists of downloading the subject files and the testing of these files, independent of the auditee's computer system. The result is computer-produced working papers that display, on a by difference basis, the results of the automatic computer processing. Eliminated is the time-consuming hand-processed substantive testing.

Another fairly recent technical development is the use of analytical auditing procedures. These procedures seek out relationships between financial aspects, between physical or operational aspects, or between financial and physical or operational aspects. This procedure infers that there are normal relationships that exist or that should not exist, and that unless they do, there may be mitigating circumstances. If not, an investigation should be made to determine why not.

This technique tends to identify areas that should be the subject of an audit of an investigative nature. Conversely, it can identify areas where little or no investigation needs be made. So it is a concept of developing more efficiency in the audit process.

Another technical area is expert systems. It is a recent development that can enhance the internal auditing operation. A computer program stores information that can be used to alert the auditor as to situations that should be investigated or to suggest audit activities that could be taken to respond to situations that have been identified as unusual.

The expert system thus functions in two capacities. First, the system can be built into the operating programs to automatically record information that, when compared to other information, will indicate a situation that should be investigated. This system is similar to a servo mechanism in a closed-circuit control system.

The second capacity is a program into which the auditor can feed information that, as a result of previous input by experienced auditors, will identify possible causes of the situation, methods of recommended audit activity and possible results of unusual situations.

Control self-assessment is a methodology that is similar to the description of auditee self-assessment I previously described. It is a technique of assembling groups of auditee personnel to identify and discuss the control procedures and processes of the auditee operation. The method has been endorsed by the Institute of Internal Auditors. As a matter of fact, it is now a section of the Certified Internal Auditor examination.

The methodology uses selected auditee representatives in a workshop to meet with facilitators of the internal staff to discuss, on an unstructured basis, the actual controls that exist within the organization and potential methods of improving them.

The next area is information system auditing. Internal auditing has used the concept of functional auditing for several decades. It has audited purchasing, budget operations, sales and marketing, various aspects of production, insurance and so forth. However, computers have become such an important part of the organizations' operations, the element of information processing itself has become a function that is deemed worthy of audit. The audit is essentially an audit of the controls exerted over the information to determine: accurate, timely and complete processing of data, safeguarding of information including data, efficient and effective operations and development and maintenance systems that satisfy user requirements.

Performance measurement is the next area. One of the scope areas of internal auditing is the determination of the efficiency with which the organization is functioning. This scope area requires that there be performance standards that can be used to compare with actual performance in order to advise management as to the operational efficiency. Normally, it would be assumed that operating management, the auditee, has these standards. If not, the auditor must work with the auditee in developing standards. The auditor will determine the validity of the standards and also determine the validity of the measurement systems that the auditee is using for comparison with the standards.

Integrated auditing is a fairly new area. It isn't new to me. When I was with the Atomic Energy Commission, we did it. It is the performance of operational or performance auditing, while at the same time, auditing the financial aspects. In the process of performing an audit of that particular function, we automatically performed an audit of the financial aspects of that function and reduced the work that had to be done at year end in the financial audit.

Environmental auditing is another relatively new area. One of the important aspects of environmental auditing is the extreme expense that's related to situations where there are problems. The Institute of Internal Auditors has developed a section and a Certified Internal Auditor examination for environmental auditing as well. It's an interesting area, and it's very important because there is so much money involved. Noncompliance with the environmental laws and regulations can cause real problems, not only because there are fines and sometimes penal issues related to noncompliance, but also because of the tremendous cost of what is called remediation or the correction of environmental disasters. Consequently, it is a new area. It is becoming extremely important. The Institute of Internal Auditors has done a lot of work in this area.

One of the interesting factors about environmental auditing is that it requires such a large group of diversified experts. In other words, in addition to the auditors, it usually requires environmental engineers, chemists, physicists and, most important, lawyers. Lawyers are recommended to be a part of the audit teams in each of the environmental areas.

Improved facilities is another area developing in internal auditing. What we're talking about is the use of electronics, which has become extremely important. The day of the columnar pad, the calculator and the ball point pen is no more. The need to travel long distances to perform audits or to station large staffs, called site staffs, in remote locations is no longer necessary. These expensive and time-consuming activities have been replaced by electronic devices that provide automated spreadsheets and other aspects of computer audit techniques. Time saving, efficiency and computer innovations allow the audit staff to provide a prompt response to management inquiries and to advise management on an immediate basis of the potential problems that must be resolved immediately.

A flat organization, which is a new development, is the elimination of the tower approach, or what is called the silo approach. In its place we have the audit direction as close to the auditee as possible. It requires that the staff be well trained at these lower levels. Today the concept even includes supervisors at the auditee level issuing audit reports without going up through the channels to the top of the organization.

Another area that has become very important is the improvement of staff competence. I think we can agree that the audit staff is the most important element in the entire audit process. It is essential that the staff be competent to conduct the audit as expeditiously as possible. It is also essential that the staff be qualified to audit in the particular areas of operation concerned as a result of training or previous experience. There are a series of rather interesting qualities that the staff should have. One is professional skepticism. Others are initiative, imagination, an attitude of cooperation with the auditee in trying to improve the auditee's operation, courage, the ability to forge ahead in spite of auditee confrontation, which frequently happens, and a strong sense of ethics.

We need to practice innovation to the greatest degree possible, innovation to effect change through the use of new ideas and new procedures. Innovation is one of the most important characteristics of the internal auditor. It provides new methods in order to accomplish efficiency and effectiveness, and it is inherent in the recommendation element of the audit findings. However, we may take this valuable concept and apply it to the entire internal audit operation so as to make it more useful to management and to the organization. A workshop that was recently conducted by the Institute of Internal Auditors identified a series of suggestions of an innovative nature, and I'll just mention a few: change in the interaction with the organization, internal restructuring within the internal structure of the internal audit operation itself, creation of new service methods and, finally, changes in the use of technology.

In conclusion, rethinking and reorganizing the internal auditing function results in a revision in its relationship to the parent organization. In the long taxonomy of internal auditing, from its early responsibility to detect fraud and clerical error, to its current general acceptance as a tool of providing management information, internal auditing is now taking its place as a part of management, though independent of management's decision-making.

Its ideal reporting responsibility to management itself, at all levels, gives it a shared sense of purpose and a common commitment to excellence. The internal auditor is no longer considered as a service functionary whose staff can, in troubled times, be victimized by downsizing. To do so would, in fact, be emasculating a part of management itself.

Also, internal auditing, though it continues to have no directive responsibilities through its findings, at times infers the direction that management should take. It becomes a sensory apparatus at all levels of management. It doesn't report abstract information, but, as a result of the application of analytical procedures applied to the results of its examination, it serves to provide management with a firsthand sense of the causes of problems and the direction or alternative directions to be taken in the resolution of situations and issues.

Internal auditing becomes a part of the executive staff of the organization. It does not serve management. It is actually an element of the management process itself. Thank you very much.

Kenneth Dye, President, Cowater, Inc., Former Auditor General of Canada

There are so many parallels between the internal audit world and the external one. Where we differ, however, is in the comment that in the internal audit world some folks are now reporting directly without a senior auditor's review of audit findings and language. I don't think Auditors General would feel very comfortable if the field auditor reported directly to government.

Let me now introduce the Deputy Comptroller and Auditor General of India, Mr. I.P. Singh.

I.P. Singh
Deputy Comptroller and Auditor General of India

I will be covering government auditing based on the experience of developing countries, particularly India. Auditing governments has always been a very dynamic process as roles of governments have been changing drastically with the times. Like any evolutionary process, government auditing in India also has been through its various stages. The stages, which epitomize the past auditing techniques were Stage I in the 1950s and 1960s, when the focus was purely on expenditure audit. Then we were talking of: sanction audit, that is, audit of expenditure as per sanctions; propriety audit, that is, due diligence and care in spending government money as if it was your own money; regulatory audit, that is, audit against rules and regulations; and certification audit.

This stage of expenditure audit was less complicated for the auditors as audit was performed with reference to laid-down guidelines, rules and regulations. The process of auditing was restricted to studying compliance of expenditure to the accepted and laid-down procedures.

Then came the second stage, in the mid-1970s and 1980s, when the focus shifted to performance audit or value-for-money audit. The emphasis at this stage was on economy audit, efficiency audit and effectiveness audit.

This stage of audit was an improvement on the earlier stage, as now the auditors were involved in the value for money of expenditure rather than just the nitty-gritty of regularity of expenditure. Here again, value for money was not a very difficult concept for the auditors to quantify, and this concept could easily be translated into valid audit observations through quantifiable auditing parameters. This kind of audit was a precursor to a system-based approach to auditing.

At this stage, we started reviewing the various government programs relating to health, family welfare, education, employment, rural development, industrial development, alleviation of the poorer people, development of backward areas, welfare of the children and women, etc. Since the government in developing countries is the key player in the development of infrastructure, i.e., roads, communication, power sector, etc., these programs were spread all over the country. Our reviews of these programs were based on value for money or 3Es audit. We have a very large public sector. Government owns a few thousand production units and companies. You name any activity, and government audit was in it (we have a staff of more than 60,000 people in the Audit and Accounts Department). We had a lot of variety in our work.

We are also one of the pioneers in the audit of taxes and revenue receipts. There are audit checks on a sample basis whether: there is compliance with the applicable tax laws; there are no apparent lacunas or loopholes in the law; or there are adequate rules and procedures designed to secure an effective check on the assessment and collection of revenue. There is also a check on the position of arrearage in tax collection is it alarming or is it reasonable, etc.

Our revenue audits have led to additional collection of revenues, a check on tax evaders and a check on corruption in tax collection, etc.

These two stages of government auditing by and large represented the theme of Indian auditing over the years until the early 1990s. Thereafter, India has witnessed major economic changes, persuading audit in India to suitably modify its approach. The various changes which have taken place in the government auditing processes in the last eight to nine years can be classified as Stage III. Auditing in this stage has proved very challenging to the auditors, as audit is being performed without any referential areas, laid-out norms and procedures. The focus of this audit is on systemic deficiencies rather than on individual occurrences.

In Stage III, some of the challenges faced by government audit include the audit of the privatization process. Privatization has been one of the important phases of the liberalization process. Audit of privatization includes need for privatization, assessment of methods of privatization, appointment of consultants for privatization, modalities of sale, disinvestment, etc. Understanding and formulating audit guidelines in this area is a great challenge to the auditors. India has a very large public sector. Its privatization is also being done gradually and carefully.

At the same time, we are trying to audit the economic liberalization process as a whole. This involves auditing the liberalization process sector-wise and commenting on performance. As this involves both macro- and microeconomic parameters, it is very challenging for the auditors to offer valid comments and suggestions in these areas, as there are no conventionally quantifiable parameters. This liberalization process has run into lots of difficulties in certain countries. We would not like to go the Russian way, as they liberalized and opened up very quickly and are now encountering lots of problems.

The other areas which are posing a challenge to us are the advancements in the field of information technology. This has been so fast-paced that it often becomes difficult for auditors to keep pace with it. Keeping abreast of the sophisticated auditing techniques to meet such work needs is a challenge to the auditors. Computerization in government agencies would be more widespread in the coming years. We have to gear up to auditing in a computerized improvement. We are heading for a paperless way of working. We will have to deal with evidences drawn from electronic data and ensure the reliability of these evidences.

Audit of the environment is another challenge, and environmental degradation has become the worry of the planet. Making valid comments and suggestions in the battle between environment versus development poses a challenge to the auditors.

We are also expected to do audit of the regulatory bodies. Liberalization has led to the mushrooming of many regulatory bodies which have become the lifeline of control in a free market environment. One of the regulatory bodies we have is SEBI, which is Securities Exchange Board of India. Even though it is a government regulatory body, the environments it regulates is the financial markets of the country which affect people at all socioeconomic levels. This poses a different kind of challenge to the auditor as he watches over not just government funds, but funds belonging to the public. We have electricity regulatory authorities. We have telecommunication regulatory authorities. How we should audit these regulatory authorities is a new challenge being faced by the Indian audit.

There is also a lot of expectation from the auditors in the field of detection of frauds and cases of corruption. Fraud offices have been set up in some countries. The auditors have to be associated with it. The expectation is that auditors should ring the alarm bells or give warning signals quickly, and not after the events have taken place or the things get out of hand.

Now there is also talk of on-line or real-time audit. Audit will have to step into auditing issues and programs on a real-time basis when these are still evolving. How can audit ensure a check on losses before they occur? How we should do on-line or real-time audit is posing another challenge.

In India, we are trying to develop, from the audit side, performance indicators which should reflect the financial health of an organization and even for the State and Federal governments. There can be many indicators like what is the government's debt position, what is the deficit in the annual budget, what is the ratio of development to non-development expenditure, what is the ratio of revenue to GDP, rate of inflation, expenditure on defense, etc.

By reading a balance sheet of a company, we can make an assessment of how sound the company is or whether the company is likely to become sick or close down in the near future. Can we make a similar assessment from the government accounts? Can we comment on the financial health of a government based on accounting information or leading indicators? Auditors are expected to work on this also.

A very important question in developing countries deals with action taken on audit findings. Since the government itself has to take necessary corrective action, sometimes they delay or try to be on the defensive. Audit is still considered a fault finder, and not seen in its constructive role. How can audit be given more teeth? How can the committees of the Congress or Parliament, what we call Public Accounts Committee, recommend and ensure quick action on the audit findings?

For effectiveness of audit, quick and stringent action should be taken on serious audit observations relating to frauds, loss of money because of inefficiency, malafide intentions and wrong decisions. In China, government audit has judicial powers. They can order recovery. They can even impose fines. Whether that system should be followed is another question of debate.

Another challenge is how to make the audit reports interesting and more readable. If the audit reports are voluminous, the legislators do not have the time to read them unless it suits them politically. In our country, the Federal audit report runs into 12 volumes and a few thousand pages. Who is going to read all this? We have to come out with a smaller booklet highlighting briefly the major findings. They can refer to the background information and details in the audit report if it evokes their interest.

There are certain sensitive areas in government audit, particularly secret expenditure. Any papers marked top secret are kept away from the auditors. There are expenditures on intelligence activities, expenditures on secret defense projects, etc. To what extent should audit have access to it? These are delicate questions.

There is a need for empowering government audit to handle situations where the executive agencies often suppress or delay production of information. This particularly handicaps government audit functions.

Some of the new challenges are like audit of intangibles. We are realizing that intangibles are also very important, such as human resources, R&D initiatives, innovation potential. How to do an effective audit of the intangibles will be another challenge to government auditors.

Other countries may have some different types of challenges because of their local conditions, but we have a lot in common as far as future and current challenges are concerned. We can jointly work out the future strategy.

Kenneth Dye, President, Cowater, Inc., Former Auditor General of Canada

Thank you, Mr. Singh. I haven't been in the C&AG's Office in India for two years, and obviously there has been a great deal of progress in the way they're approaching the challenges of auditing one of the largest nations on earth. One of the points you made was the importance of getting the auditor's message across. I recall when I was Auditor General, I was reading a periodical out of the United States that said United States legislators in both State and Federal politics don't like to read very much. Somebody did a survey, in a university, and they concluded that legislators read nine minutes a day and talk or listen the rest of the time while they are awake. So I caught onto that, and so did the GAO. Instead of producing written audit reports, we produced videos. The public servants didn't like it very much because it was too punchy and not enough context, but it got the message across. The one thing that I wanted to do, and you may take this as a challenge back to India, I always wanted to do my audit reports as cartoons. My professional colleagues really couldn't agree with me, and I never did publish a chapter in cartoons. Although I got a lot of cartoons of myself, I was never able to publish a cartoon book on auditing. It's an opportunity. Perhaps, maybe legislators would read cartoons.

Let me move along to our wrap-up speaker, Mr. Peter Armstrong.

Peter Armstrong

Technical-Administrative Director of the INTOSAI Development Initiative for the OLACEFS Region and Former Director of Special Projects at the Canadian Comprehensive Auditing Foundation

Conference President Jim Wesberry, Ken Dye, panel members, ladies and gentlemen, good afternoon. It is an honor and a privilege for me to have been invited to Washington by Jim Wesberry, to participate in such an important event.

Recognizing the presence of about 40 people from 10 Latin American countries, and the fact yesterday that some of the speakers from those countries spoke to us in English, to try to effect a kind of balance, I would like to make my small speech in Spanish, language of the gods. So I ask for your patience with my linguistic weaknesses, and your forgiveness if I commit some grammatical errors (or horrors!).

First, I'd like to thank Ken Dye for having helped to launch my career as an international consultant. About ten years ago, as Auditor General of Canada, he allowed me to carry out my first consulting assignment in the private sector, when I reviewed the SAFCO Plan, developed by Tony Sanchez. It was in Bolivia, as well, that I met Jim Wesberry for the first time. (Note: this is untrue, as Jim later pointed out, as we had met when he was at the OAS.)

Now, to the topic at hand. In the few minutes available to me, I will discuss two distinct but related topics. First, I will discuss the challenges facing the legislative external auditor the SAI in the future. I have become aware of some of them in my travels in the world, especially in Latin America. Second, I will comment briefly on what the INTOSAI training organization the INTOSAI Development Initiative (IDI) is doing in order to solve some of the identified problems.

The challenges: I know that what I'm about to say in the next few minutes about the challenges facing government external auditors implies a comparison of what exists with what I consider to be an ideal situation. I know that changes such as I am suggesting cannot be made overnight. Each country has its own culture, its own history, and each SAI has been established within the context of its own reality, culture and history. Also, I am not going to suggest how to effect the changes implicit and suggested, as the solutions have to be tailor made; they cannot and should not be developed by foreigners. I'm not going to focus on the changes that are taking place outside the SAIs, and that have a tremendous impact on their work, but rather on where I see that existing paradigms the established patterns should be changed, as they impede the work of the SAIs.

First and foremost, the SAI should think about its raison d'etre, its role as a change agent and promoter of transparency within a democratic society, and its place within a modern accountability framework in the next century. This will involve some radical changes in mentality and culture and implies, for sure, educational programs for elected representatives, for the mass media and for the citizens.

First, the SAI should enjoy real independence. Above all, the SAI should be completely independent of the executive branch of government. For example, where it is positioned under the Minister of Finance, or even under the President of the country, its mandate cannot be carried out independently, especially when it comes to that Ministry or the Presidency, both of which should be subject to audit by the SAI. Once an SAI is involved in any governmental process, its independence disappears or at least is compromised, or seen to be compromised, limiting its effectiveness and credibility.

I know that some SAIs are still involved in various administrative processes of their governments, and with good reason. But this is not to say that the SAI could not, at an appropriate moment, suggest that these responsibilities be transferred elsewhere, to other government entities. This tendency, I would imagine, comes from the era when the SAIs were first established, and their primary role was to review and approve proposed government expenditures. This involvement in administrative processes can be in the form of pre-audit, preapproval of capital expenditures over certain amounts, approval of certain aspects of personnel hiring, approval of plans and reports of internal audit, and training of public sector employees.

Many of the world's SAIs, from the moment of their creation, have followed the same trajectory, beginning by carrying out this pre-control function that was their reason for existing. Given these beginnings, it doesn't surprise me that the terms "control" and "controller" arose, and which are used instead of "audit. These terms have always confused me, as I never know, for example, whether one is speaking about "internal control" or about "internal audit. I've also heard a variety of other terms to describe "audit, such as "supervision, "monitoring, "vigilance, and "fiscalization.

For me, the term "control" implies that someone is involving themselves in a process, "controlling, in one way or another. For this reason, I always refer to the role and work of the SAI as being "audit. Also for this reason, the name of my private corporation is "Audire, like "audit, which comes from the Latin word "to listen, to indicate that the role of the SAI is to listen and inform/report, and not to involve itself in any way in administrative processes. The real power of the SAI comes from auditing and reporting, not from "controlling.

Most SAIs have given up the pre-audit function. As I said a few moments ago, involvement brings with it compromise, and can lead to loss, or perceived loss, of independence. The trends in the SAIs of the world have been toward greater independence, and away from involvement in administrative processes.

The SAI should be free from political forces and influence. For example, appointment of its senior management and its leader, as well as its employees, should not be made on the basis of political affiliations, but on knowledge and experience in the field of audit and/or government.

It's worth pointing out that in advanced SAIs, audits are carried out by multidisciplinary teams, comprising professionals from diverse disciplines, depending on the nature of the entity, program or activity being audited. What's important is that the members understand the audit discipline.

I hardly dare to touch on the next point, but the SAI should not be involved directly in "citizen participation" programs, where communication of complaints about government malfeasance and poor service is made directly to the SAI. It would be far better if a separate government agency, or separate unit or department within government ministries, were to carry out this function. When handled in this way, where the SAI is not involved directly, the SAI can audit and report to the legislature and to the public, about how well this service is functioning.

The SAI should be able to make its own audit plans, taking into account only those suggestions of the legislative members and the public that it wishes, within the context of its long-term and operational strategies and plans.

The Head of the SAI's term should not coincide with the comings and goings of governments, to avoid the possibility of being seen as a political tool or worse, a political weapon of the government. The term should be for between five and ten years, so that the Head can do his or her work with maximum efficiency and effectiveness. One does not learn to be an Auditor General overnight!

The SAI should have a broad-scope mandate, to allow him/her to carry out value-for-money audits (also known as performance, operational and results-based audits), and should have appropriate staff to carry them out.

As we heard from Bob Elliott, users of the reports of audit entities in the private and public sectors are demanding a wide range of information about the results of activities and programs that go far beyond the traditional financial audit, which is now, from many points of view, obsolete. The new reports, on management and performance, will have to be audited by the SAI (in the government setting), and legislative auditors must prepare themselves for this inevitability.

On another sensitive point, the SAI needs continuity and homogeneity as regards the succession of its Auditors General. I have seen, with some frequency, situations where an economist as Auditor General is succeeded by an engineer, then, at the end of that term, by a lawyer, then by an accountant/auditor. With all due respect to all these professions, a SAI should seek, at least at least a homogeneity as regards the profession of its Head. The confusion, the change in direction, can be so dramatic as to almost destroy the SAI during these transitions.

Also, I have seen a tendency among new Heads of SAIs, knowing little or nothing either about audit or about government, to try and reinvent the wheel, wasting enormous amounts of public resources and time developing a new label for a bottle of the same wine. Or worse, not only is a new label developed, but also a new wine, which can turn out to be vinegar!

The SAI should have the independence to not only audit and report on any government entity, it should also have the freedom to report widely to the media and the general public without any political or government interference.

Audit reports should be easy to read (or accessible, as Tony Sanchez said yesterday). That is, they should deal only with issues that are important to the government, the legislature and the citizen, and should be written in a simple, easy-to-understand style, even though they deal with complex issues.

To increase their accessibility, they can be published in electronic form, or as videos, or made available to the whole world, via the Internet.

On another point, there are those who maintain that any illegal act discovered is of equal importance and should be reported. Please! Please!! The Head of the SAI and his/her professional staff must, at all times, exercise professional judgment, in deciding what to report, but using reasonable criteria, which are applied evenly to all the reports.

Findings/observations that are not of interest either to Congress or to the public should be reported directly to the audit entity in management letters, and not clutter up reports to the legislature.

That is, the SAI should think about client needs (once it has been decided who is the client(s)!), in the development of audit plans, programs and reports. One has to question the usefulness of a 500-page report that is totally ignored. Of what use is a report that deals with trivial matters, sent to Congress? Who will bother reading it? Of what use is a report that is ensconced in such legalese and is so difficult to understand that its accessibility approaches zero?

Another point: Even where the legal aspects of audit have been officially downgraded in importance (in favor of real auditing), one of the indicators of good performance in those SAIs remains the number of illegalities discovered by the auditor, without regard to its relative importance (or even stupidity!). This implies that the culture within the SAI has to change. No easy task, as we heard yesterday.

For example, as Tony Sanchez told us yesterday, there was a case in Bolivia where a number of children died as a needed vaccine was not allowed into the country, as a minor, obscure legal point had not been complied with. Another case of which I am aware involved a town mayor being penalized by the SAI, for breaking the law. What had he done? Instead of using public funds for approved purposes (road maintenance and repairs), he had the made the very wise and humane decision to feed starving children. For this he was punished?

Another example that points up the pitfalls of emphasizing discovery of legal infractions as a criterion of good performance by the auditor: In a country that shall remain nameless, where the auditor discovered that a supplier had been purposefully overpaid under a kickback scheme, the auditor scored high, as not only were the guilty parties penalized, the clerk who wrote the check and the cashier who cashed the check, both of whom knew nothing about the real situation, were penalized as well, to enhance the auditor's score.

I also believe that, where the audit team discovers legal noncompliance, the issue should be followed up by either a special legal audit team within the SAI (better) or by a different organization entirely (best). In this way, the audit team can concentrate fully on the task at hand: auditing!

Today, the basic element of control in an organization that has empowered its staff to make decisions, is a group of fundamental rules. These rules reflect the philosophy, its values, its management principles and a code of ethics/behavior. Based on an analysis of existing business risks, limits are established within which employees can make decisions. The rules are few, but firm. Violation attracts sanctions.

The SAI that focuses solely on numeric-legal auditing (or control) should prepare itself for the day when few legal controls exist in the traditional sense. When these very numerous controls disappear (the tendency worldwide), what will the narrowly-focused auditor do?

I don't want to start a war, but one day I would like to study the relationship between the type of SAI and its work, and the level of corruption in various countries. Although there are undoubtedly many other factors, I'm convinced that those SAIs that successfully confront the challenges mentioned above, over the years and decades, will contribute, in a significant way, to the reduction of corruption in a significant way.

There is also the danger that the SAI may become enamored of databases, either created within the SAI from information provided by the audited entity, or by going on line, with real-time connection to client systems and data. There is the risk or danger that the auditor will then try to carry out his work by staying in his office, making micro- and macroeconomic analyses of client performance.

Some SAIs have, or are in the process of developing, large databases on client activities, which imply enormous costs, not only by the SAI in the design, development and maintenance of the required systems, but also on the part of the client, which has to provide information that is costly and superfluous, without any real use for them, in order to satisfy a requirement of the SAI, and whose benefit is doubtful, to say the least.

If the SAI demands that the client provide information that the SAI then inputs into its own EDP systems, the information will either be received late, be input late, be incorrect, or not in sufficient detail to be of use. The result is a lot of effort and resources being invested in systems of dubious worth.

Please, don't become enamored of databases as such. The only way that an audit can be done effectively involves the auditor acquiring and keeping up to date, an in-depth knowledge of the client business, plans, problems, changes, and risks, etc., by doing his work in the field, on the client's premises, in constant dialogue with client management and staff.

In the past, both external and internal auditors tended to note errors, fix blame and report to management. The typical impression among administrators was that the auditors were "those who come into the office, waste everyone's time, and criticize all that you do. Or, "The auditor is the guy who enters the battlefield after the war and shoots the wounded." As someone once said, "The two biggest lies in the world?" Lie No. 1: "Good morning, I'm the auditor. I'm here to help you." No. 2: "How nice to see you! Do come in!"

The process as I've described it is not appropriate today. The audit cannot function in an atmosphere of combat of attackers and defenders. Today, audit should be seen as an important and positive part of the global system of control, within a framework of government accountability.

Training: You can see from the points I have touched on that there is a very strong, positive and permanent role that training can play in any SAI. I'm talking not only of technical and related training for audit professionals, but also about educational and awareness programs for the public, for Congress and for the media about what is the proper, positive and essential role of a SAI within a democratic framework. In this ever-changing world, constant training and education is of fundamental importance. I don't have to reiterate the obvious about the changes that are impacting governments and their SAIs, as you are all well aware of these.

To deal with worldwide training needs in SAIs, more than ten years ago, Ken Dye, with the then-Comptroller General of the United States, Charles Bowsher, established the INTOSAI

Development Initiative IDI. They were both aware of the enormous amounts of excellent training materials and skills available in the SAIs of developed countries, and the equally enormous needs in those of developing nations. (Although I use the terms "developed" and "developing, I don't like them, as they imply something pejorative about those countries that are developing. This is not my intention.)

The need for training has not changed over these years. With rapid advances in the field of audit, and the increasing sophistication of government activities, programs and systems, and public demands for better service at lower cost, training becomes even more important.

From its establishment in 1986, IDI has been attached to the SAI of Canada, and has presented more than 100 workshops, involving more than 155 SAIs, in over 55 different countries, in four of the official languages of INTOSAI. Until now, IDI has focused on the presentation of workshops on technical subjects, from human resource management to use of computers and statistical sampling in the audit process, and value-for-money (also known as performance, operational, management or results-based) auditing.

This effort required the dedication of significant resources by way of contributions in kind by the SAIs of the many countries involved, in terms of training needs analysis, design, development and workshop delivery, as well as acting as host SAI for workshops.

Before being transferred to Norway in the year 2001, IDI is implementing, in seven of the regional groups of INTOSAI around the world, a Long-Term Regional Training Plan (LTRTP).

The LTRTP is designed, up to a certain point, to help SAIs successfully meet the changes taking place in the world. More specifically, the Plan is designed to give audit professionals in these organizations an increasing variety of knowledge and skills needed to successfully deal with emerging and complex audit problems, such as those posed by the information revolution, global concerns about the environment, public sector reform, and the menace of public deficits and debt.

The objectives of the LTRTP are: first, to assist SAIs, individually and as regional groups, to strengthen their training capabilities within a relatively short time; second, to provide a means of broadening the scope of regional and local training activities that will help the SAIs successfully manage the ever-increasing number and complexity of the challenges facing them.

These objectives will be accomplished primarily through the establishment or reinforcement of "training infrastructures" at the regional and local levels. This should ensure, particularly at the regional level, the viability and sustainability of training activities over the long term.

One of the primary products of the LTRTP will be the training, in a profound and broad way, of up to 25 auditors in each of the seven regions (including OLACEFS), in the areas of needs analysis, course design, development, delivery and evaluation of training courses.

To achieve this, IDI's LTRTP comprises four workshops: (1) a workshop on Strategic Planning for training (one week); (2) a Course Design and Development Workshop (CDDW) on the design and development of training courses (eight weeks); (3) a workshop on training (classroom) skills (four weeks); and, (4) a regional workshop on a technical audit subject.

The Strategic Planning Workshop (which took place in Lima in June), was a consultative process with the highest-ranking personnel from SAIs of the OLACEFS region. Its primary objective was to discuss the LTRTP in order to achieve a basic and common understanding of its goals and objectives, and to agree on ways of adapting and implementing it in the OLACEFS region.

The results of this workshop, under the strong leadership of Dr. Victor Enrique Caso Lay, Controller General of Peru and President of OLACEFS, were a number of decisions, including: an agreement on the need for, and elements of, a regional training infrastructure; general guidelines for training for the region and requirements for participation in the Program; identification of the key requirements and priorities for training in the region as a basis for developing a regional training plan; an understanding of the key roles and responsibilities; and an action plan that describes the steps to be taken to launch the program.

This program is in its advanced stages in almost all of the INTOSAI regions in the world. In fact, it is almost completed in the English-speaking AFROSAI region of Africa, and with great success, under the strong leadership of the Auditor General of Zimbabwe, Eric Harid, who is with us today.

For this Program, in the OLACEFS region, IDI is seeking financial support from the Inter-American Development Bank, which generously supported all of the first phase of IDI's work in the region, and the first workshop of the Program just outlined the Strategic Planning Workshop.

The purpose of the second workshop under this Program the Course Design and Development Workshop is to train 25 audit professionals, from all countries of the OLACEFS region, in the analysis of training requirements, the design, development and administration of courses, and in the evaluation of training activities.

In the first three weeks of this workshop, participants will be exposed to the concepts and practices of adult education, and will individually apply them in the design of short, two-day workshops on topics of interest to their respective SAIs. In the second part of this workshop (five weeks), the participants actually design and develop two, two-week workshops, on topics identified as regional priorities during the Lima Strategic Planning Workshop (described earlier).

Assuming that funding is obtained, it is our intention to present this workshop in early 1999.

The four-week Train-the-Trainer Workshop is planned, tentatively, for the latter part of 1999, and will be attended, hopefully, by the same people that attended the previous eight-week CDDW workshop. In this workshop, participants learn: (1) how to teach adults in the context of a professional audit environment; (2) how to effectively use interactive training techniques, i.e. techniques that maintain a certain desired level of student participation in order to maximize the learning that takes place; (3) how to evaluate pilot presentations of courses and how to revise the course design, as appropriate; and, (4) how to evaluate instructors. It should be pointed out that in this workshop, each participant, in turn, will present sessions from one of the two workshops developed in the eight-week CDDW described earlier.

The last activity is the presentation of this piloted and revised course, by three or four of the 25 participants, to a regional audience of professional auditors from the SAIs of the OLACEFS region.

And why all this effort? To ensure that all training is focused on better audit performance by the SAIs, and that it relates directly to the real needs and priorities of the SAIs, with the aim of strengthening and enhancing transparency and accountability.

Not only, as Tony Sanchez said yesterday, can there be neither accountability nor transparency without democracy, but also, looked at in another way, there can be no real democracy without accountability and transparency.

We should bear in mind that modern legislative audit is the continual analysis of risks, and the constant search for improvements, and ensuring that audits are duly completed on a timely basis, providing benefits to the audited entity, with valuable information for congress/parliament and the citizens it represents.

But the most important benefit of all of our audit efforts takes place when we conduct excellent, professional and independent audits, and when we inform government, elected representatives and the citizenry about all that we have identified, as auditors, as being of significance. This system of accountability promotes increased confidence of the voters in any country, in the transparency and honesty of government an essential ingredient a cornerstone in a democracy.

To conclude, I would like to quote a former Auditor General of Canada, "In a democracy, accountability is the price exacted for the gift of power."

Or, as Simon Bolivar said, centuries ago, "The public wealth does not belong to those who govern. All those who have been entrusted with the wealth of the citizenry have the obligation to disclose fully the uses to which this wealth has been applied.

MR. DYE: Are there any questions of our speakers?

MR. HUGHES (United States): In the United States, our internal auditors are not required to be certified, nor are our government auditors that do financial auditing required to be certified or licensed. In the private sector, we would never permit that to happen. Is it just an anomaly that we have that with government auditing? Is there any movement in any other nations to require certifications or licensure or continuing professional education?

DR. DITTENHOFER: Several States in the United States have provided that the auditing should be done by Certified Internal Auditors. That's about the only thing of which I'm aware.

MR. DYE: I'm not aware of anything internationally. The CIA designation is becoming an international designation. You see the odd person in developing countries with that designation. With respect to auditors in SAIs, you almost have the reverse. For example, in Germany, when a professional accountant goes into government service, they lose their CPA or the CPA equivalent in Germany. They are no longer considered a professional accountant.

DR. DITTENHOFER: The task force that I mentioned yesterday that's working on the Internal Audit Standards is grappling with this question now. They're trying to come to some conclusion regarding certification for internal auditors.

MR. DYE: My sense is that certification is a North American thing, and you don't see as much of it in developing countries. Certainly in the supreme audit institutions, few of them have people with professional designations. They do have some, but it is a smaller part of their populations.

MR. HARID (Zimbabwe): Maybe just a contribution from Zimbabwe. The situation in Zimbabwe is a little different in that we have an umbrella body that encompasses the CA's as well as the public sector auditors. They have a certificate for public sector auditors. I have one, so we can say in Zimbabwe that we've managed to accomplish what the U.K. may not have been able to accomplish. We have a mother umbrella body for the accounting professions in the country.

MR. DESTA (Ethiopia): Similarly, in Ethiopia, the Office of the Auditor General mandates that internal auditors are certified before they're assigned as internal auditors in various governmental organizations. So, in our office, we do sanctify internal auditors particularly before they are assigned as Chief Internal Auditors. In addition, we have recently established a chapter of the Institute of Internal Auditors of Florida. We have legalized that organization and the number of members applying is actually increasing. So in Ethiopia, we certify internal auditors before they're assigned to the position of Chief Internal Auditor in government institutions.

The Annual Financial Report of the United States Government

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Good afternoon. What I'd like to do this afternoon is go through the process that we followed in preparing the consolidated statements for the United States Government. In going through that process, I want to talk a little bit about the background, what led to the financial statements, what are some of the requirements under which the Federal government operates. I also want to talk a bit about the purposes and the limitations of the statement. I'd like to go through the preparation process, describe some of the highlights of the statement, and finally, conclude with what we saw as some of the benefits of the statement.

In professional sports, you always like to see ball players leave their sport, whatever it may be, at the height of their career. I feel that leaving Federal service right after I got this statement out, was like a ball player leaving at the height of his professional career. Even though we didn't get a clean opinion, the fact that we were able to get the statement together and get it out within the statutory due date was quite an accomplishment. As someone has said, it took us 200 years to get to that point.

Just as a sidebar before I go into the presentation, the President in his 1999 budget submission indicated that it was the Administration's goal to get a clean opinion on the government-wide statement by Fiscal Year 1999. That's quite a formidable challenge for those who remain in the Federal government. Our good friends at the Department of Defense are one of the reasons why we may or may not be able to achieve that goal.

When one looks at this process of preparing the government-wide financial statement, you have to start at the foundation, the Constitution. The United States Constitution requires a regular statement of accounts. Receipts and expenditures of all public money shall be provided or published from time to time. So the Constitution had a requirement that elected officials of this government be accountable to the citizens by publishing this account of receipts and expenditures from time to time.

Well, the Department of the Treasury, took that responsibility very literally and they did fulfill that responsibility by preparing what was called The Annual Report. It was a document that came out on a yearly basis, but it was basically a cash-basis document. The document only showed exactly what the Constitution required, i.e., the cash collections and the expenditures. It also showed the Federal government's cash position, but that was all it showed, i.e., cash receipts, cash disbursements and the cash position of the Federal government as of the end of that particular year.

Unfortunately, the document did not include information on the Federal government's assets, such as its property, plant and equipment, its receivables or its liabilities. As all of us know, without reporting liabilities, you really are not disclosing the true condition of any entity. So, the Federal government's reporting was sort of like our checkbooks   a cash-in and cash-out reporting. We never disclosed in a coordinated fashion what our true costs were or what our liabilities were, and what kind of costs were associated with the political decisions being made. In many cases, those costs were being incurred much later down the road, and not reflected in the cash receipts and disbursements during the particular period. So, that was sort of the context or the background that we were operating in within the framework of our guidance from our Constitution.

In about 1975, the Department of Treasury started preparing a prototype financial statement. One might say, How could you be preparing a prototype for 20 years? That's what was going on 21 years, to be honest. The Department of Treasury started preparing prototype financial statements for the Federal government in 1975, and they prepared one every year until 1997. In 1997, of course, we prepared the actual consolidated statements that were subject to audit.

A lot of the credit for keeping that dream of a consolidated financial statement alive goes to Jerry Murphy who recently retired from the Department of the Treasury. Many of you probably know Jerry. Jerry, through a lot of perseverance, kept the idea alive of a government-wide financial statement. Frankly, a lot of the elected officials in this government, as well as appointed officials, didn't want to see what an audited financial statement would show. People sometimes don't want to know the true costs of their programs. Thanks to Murphy's insistence, the thought was kept alive. It didn't get a lot of publicity, but at least it was kept alive.

The prototype statement had its shortcomings. Treasury asked the various Federal agencies to provide the information voluntarily. If agencies didn't provide certain information, the Treasury Department would estimate the information based on information they had. So there were some real questions about the reliability of the information that was included in that prototype. Nevertheless, it kept the dream alive. This prototype was operating from 1975 until 1996. The driver or the engine that really drove the preparation of a government-wide consolidated financial statement was a series of management reform laws that were passed in the 1990s.

The first one of those financial reform laws was the Chief Financial Officer's Act, passed in 1990. The Chief Financial Officer's Act required audited financial statements for certain major departments and agencies. It was the first time the Federal government required certain components of the Federal government, its major bureaus and agencies, to prepare and have audited financial statements. In addition to requiring audited financial statements, it established the position of Chief Financial Officer in each of the major departments and agencies. Prior to that time, the responsibility for accounting and financial management in each of the agencies was a disbursed function and it wasn't always centrally located. The individual with that responsibility wasn't always sitting at the highest levels of the agency. The CFO's Act brought all that together.

Concurrent with the adoption of the CFO's Act was the establishment of the Federal Accounting Standards Advisory Board, FASAB. FASAB's responsibility was to consider and recommend accounting standards tailored to the Federal government's unique characteristics and special needs. That's important, because there was a great deal of controversy when FASAB was established. Within the United States, we have the Financial Accounting Standards Board which sets accounting standards for the commercial sector, or for private organizations. We have the Government Accounting Standards Board which sets accounting standards for State and local governments. There were those that said, Why do you need a third standards-setting body? Well, let me tell you. Nobody in those other two bodies have to account for things like weapons systems, or the Washington Monument, or these heritage assets that make up our national treasure. The unique accounting requirements of the Federal government required a unique set of accounting standards. FASAB was established to address that need.

By the end of 1996, FASAB had completed work on a comprehensive set of accounting standards for the Federal government. Without that, the preparation of a government-wide financial statement would have been very difficult because we did not have consistency in terms of the accounting principles followed by Federal agencies. We had a hodge podge. People were following commercial standards in some cases, their own policies and procedures in other cases. There really wasn't any glue. So the FASAB's comprehensive set of accounting standards gave us the foundation of accounting policies to follow when preparing the government-wide statement.

It's hard for some people to accept or believe that until FASAB completed work on its standards, the Federal government, the largest entity in the world, did not have a comprehensive set of accounting standards to follow. Some of you may find that a little amazing. My friends in the public sector, where I am now, never realized that the Federal government didn't have a set of accounting standards to follow. They never realized that Federal agencies didn't prepare an annual accounting for elected officials and citizens. People just took for granted that kind of reporting existed. It didn't. The primary focus of financial management in the Federal government was to get your appropriation for the following year, and make sure you didn't overspend your budget for the current year. There was little concern about control over assets and liabilities, or reporting those assets and liabilities. Once again, it was checkbook accounting. How much do I have and how much can I spend? As a result, we have major liabilities that have been undisclosed. We'll talk about those in a moment. So the second financial management reform was the establishment of FASAB, the Federal Accounting Standards Advisory Board.

The third element of these financial management reforms was the Government Management Reform Act (GMRA). The Government Management Reform Act basically amended the Chief Financial Officer's Act. The Congress, seeing the results of the experiment to prepare agency-wide statements with respect to some of the agencies and departments of the Federal government, liked what they saw and decided that every one of the major agencies in the Federal government had to prepare and have audited an agency-wide statement. That's what GMRA did. The Congress said, Oh, by the way, not only do each of the major agencies have to prepare and have audited agency-wide statements, but the Federal government as a whole has to prepare and have audited a government-wide statement. Congress placed responsibility for preparing that statement with the Secretary of the Treasury, and the responsibility for auditing that statement with the General Accounting Office. GMRA sort of closed the circle. We started with a CFO Act that said pieces of the Federal government will have to prepare financial statements and have them audited. FASAB gave us the accounting standards to follow in that process and GMRA closed the circle by requiring a government-wide statement to be prepared and audited.

On top of that, President Clinton, when he took office, initiated an effort called the National Performance Review. While all this was going on, the National Performance Review in its work came to the conclusion that the American people require more accountability from their government. The elected officials in this country should be more accountable for how they spent the public's money. And the National Performance Review, independent of all other efforts, recommended that the Federal government prepare a government-wide financial statement, and have that financial statement audited. We had this confluence of events leading up to the preparation of the first-ever government-wide financial statement.

I'd like to talk a little bit about the purpose of the statement and some of the limitations of the statement. Clearly, one of the purposes of the statement is to demonstrate accountability. Up until recently, we were collecting $1.7 trillion and spending $1.9 trillion or so. The point is that up until we had the requirement for agencies to prepare financial statements, there was no after the fact reporting of how the money was spent. There is actually a column in the budget to do this, but don't go to the bank with it. You wouldn't want to risk your professional reputation on the accuracy of the actual column in the budget. So, the point is there was no after the fact reporting to the American people of how their tax dollars were spent. With the CFO's Act and with the government-wide statement, one of the objectives was to inform the American people about how much money was collected and how it was spent. One of the clear objectives was to demonstrate accountability.

The second objective is to establish some fiscal discipline within the financial management community in the Federal government. Again, as you all know, the discipline of an audit does wonders for helping to clean up the problems you may have in your financial management operations. Without the audit, you have a tendency to not be as careful as you might otherwise be. Let me give you an illustration. Before financial statements were prepared in the Federal government, the Internal Revenue Service, which is our tax collecting agency here in the United States, would tell Congress each year that it had accounts receivable of somewhere in the neighborhood of $175 billion. In other words, if they collected all the taxes that were due them, that amount would be $175 billion. Using that number, they would march up to Congress every year and get additional appropriations to carry out their activities. Well, the first year their financial statements were audited, that $175 billion turned out to be $65 billion, and of that $65 billion, only about $30 billion was actually collectable. So, the point I'm trying to make is that audited financial statements have a wonderful way of shining light on some of the numbers that are being bandied about in the political process.

This fiscal discipline was clearly one of the objectives of the financial statements. Early on in this process some people made the mistake of trying to sell financial statements as a management tool, that people actually made management decisions based on the financial statements. That's a big mistake. Nobody ever makes a management decision based on a statement that comes out six months after the year is over. But the idea is if you can produce accurate numbers to present in that financial statement, your underlying systems are producing accurate, reliable numbers. Those are the numbers you use to make your day-to-day management decisions.

One of the major limitations of the statement is we still have a bit of a problem with respect to the reliability of the data. I'm not going to stand up here and tell you that the data was pure and clean the first time out of the gate. I don't think anybody has ever been successful in having a clean opinion or clean data the first time around, especially in an entity as large as the Federal government, where for 200 years we didn't care about our assets and liabilities.

Another limitation of the statement is that there are certain assets and liabilities of the Federal government that are not reflected on the statement. The debate right now is Social Security. Is that a liability or not? Right now it's not on the statement as a liability. I think everyone that is waiting to collect a pension from Social Security considers it a liability, but the policy makers don't. Leaving Social Security aside, the financial statement does a pretty good job of recognizing what the Federal government's liabilities are. Where it falls short though is in recognizing all the assets of the Federal government. One of the biggest assets you can't put a value on is the government's sovereign power to tax. The fact is that if the Congress and the Administration had the political will, and the people wouldn't revolt, you could raise taxes and you could wipe out the deficit. There is no comparable thing in the private sector. There is no recognition or measurement of that power to tax. That's a huge asset.

There are other things that are not recognized in the Federal government's financial statements. The Federal government owns vast quantities of land that has no cost. It was acquired or stolen from the Indians, or acquired for nickels and dimes. The land has value but there is no cost associated with it. It's not reported on the balance sheet as an asset. It is reported in a separate section of the financial statements called the stewardship section. FASAB created, under the accounting standards, a separate reporting section called stewardship reporting. It was intended to show some of the things that the Federal government owns for which the Federal government has a stewardship responsibility. Not necessarily can those items be reported in the same way as traditional assets. The Federal government's heritage assets, i.e., monuments, national treasures and things of that nature, are reported in the stewardship section.

A glaring gap that needs to be worked on is that the statement includes all the activities of the executive branch, but not the judicial or legislative branches. We operate with three branches of government, but because of constitutional separation of powers, the executive branch cannot compel either the legislative branch or the judicial branch to do anything. They basically operate on their own. So we have missing assets. We have revenue and expense information from the legislative and judicial branch, but we do not have their assets or liabilities.

The legislative branch's assets are minuscule. They are not major and they are not material. But the judicial branch's assets are substantial. It's all the Federal courthouses located throughout this country. That's a large chunk of our real property. Those are not on the statement. Those are some of the limitations with respect to the statements.

Let's talk a little bit about the preparation process. Those of you who are familiar with the audit process know that any time you're auditing an entity, one of the requirements of the audit standards is that you get a legal representation letter from the entity's counsel, and a management representation letter from the Chief Executive Officer of the organization and the Chief Financial Officer. The General Accounting Office, being the guardians of the audit standards that they are, when they did the audit of the Federal government's financial statements, they required a legal representation letter and a management representation letter. Who in the heck is going to sign the management representation letter for the Federal government? The idea of a management representation letter is that the letter should be addressed to the auditor and signed by members of management whom the auditors believe are responsible and knowledgeable directly or through others in the organization, about matters covered in the representation. The Federal government is so vast and so decentralized that there is no one person who is knowledgeable of all the financial management activities of the Federal government.

Another thing that was difficult in the negotiations for these legal and management rep letters was what the heck would the management rep letters say? We finally resolved the impasse; we had the management representation letter signed by the Deputy Director for Management at the Office of Management and Budget because he is the Chief Financial Officer of the United States, under the Chief Financial Officer's Act. As far as the Chief Executive Officer, none of the political leadership wanted to sign it. None of them. The gentleman that eventually signed it was Jerry Murphy. He was the Fiscal Assistant Secretary in the Department of Treasury. Jerry Murphy was the guy who was ultimately responsible for preparing the statement. It was delegated down to his level. Jerry signed the management rep letter as the Chief Executive Officer. It was kind of an interesting exercise. You wouldn't believe how fast the political leadership ran away from this letter. Nobody wanted to put his or her hands on this management rep letter. Nobody wanted to touch it.

The legal representation letter, that was also a difficult exercise. There, what we ended up doing was we had the Assistant Attorney General for Administration sign the legal representation letter. But his representation was based on information provided to him from each of the general counsels throughout the government, from each of the executive departments and agencies. What we ended up doing was a compromise, but we got the letters, and GAO was happy because they were able to comply with the standards. That was one of the first steps right out of the gate that we had to overcome in preparing these statements.

The second challenge in the preparation of the statement was the manner in which the standard general ledger was implemented. We talked about the fact that each of the major agencies prepares and has audited financial statements covering all their activities. Well, we didn't just take the 24 major agencies, roll them up and do the consolidated statements. There was a whole series of reasons why that wasn't done. In any event, that was the choice that the Treasury Department made.

In the Federal government, each agency has an individual appropriation account covering certain activities. Some agencies may be funded by one appropriation account and other agencies may be funded by 35 or 40 appropriation accounts. It is a function of the interplay between the executive branch and the Congress and their appropriation committees. By virtue of having these individual appropriation accounts within each agency, it gives individual members of Congress a great deal of power and authority over limited activities of a particular agency. The structure that was in place enabled Treasury to accumulate information by individual appropriation accounts. Therefore, each agency submitted to Treasury a trial balance for each of its appropriation accounts. None of this could have been done without the implementation of a standard general ledger.

The foundation for this whole process is that the United States Federal government has a standard general ledger with standard account codes and standard definitions for every agency in the Federal government to follow. I won't stand up here and tell you it is 100 percent implemented. But if you do not implement the standard general ledger, at a minimum, you have to be able to cross walk whatever you have to that standard general ledger. Without that standard general ledger, this process could have never been accomplished. We would never have been able to do this without the standard general ledger.

With that as the foundation, each of the agencies submitted to Treasury, following the standard general ledger, their individual trial balances for each of their appropriation accounts. Treasury rolled all this information up, and that was the basis for the beginning of the process the beginning of the process of consolidating the information to prepare the consolidated statements.

There was a verification process as well. You may say to yourself, You have individual agency audited financial statements. Each of those statements was audited. Then you're rolling this stuff up under a different basis for the consolidated statements? What Treasury did is it aggregated the individual appropriation accounts by department and agency. They provided that information back to the auditors of the individual departments' financial statements, and said, Compare this aggregated information that we got from the agency with the financial statements that you audited and tell us if there are any differences. That's how the data was verified. As you might imagine, there were some differences.

Think of this as a huge worksheet of thousands of appropriation accounts all being aggregated to make up this consolidated total. There were some problems. I'm not going to stand up here and tell you that the first time through it was a piece of cake.

I'm going to talk about some of the gaps in the submitted data. As I said earlier, we don't have information on the real property of the judicial branch. Another problem is eliminating intergovernmental transactions. The Federal government does a huge amount of business with itself. We have the General Services Administration, for example. Each of the Federal agencies pays rent to the General Services Administration. The General Services Administration then goes out and negotiates leases with private landlords. The General Services Administration buys supplies and equipment from private vendors and sells those supplies and equipment to each of the Federal agencies. So you have revenues and expenses there that need to be eliminated. You have agencies supporting one another by engaging in transactions with one another. Guess what, nobody ever identified how much business they did with other Federal agencies, not to mention who they did business with. So it came time for us to aggregate all this. When you're aggregating financial information and your goal is to consolidate it, you need to eliminate the transactions you have with yourself.

Well, we were unable to eliminate those intergovernmental transactions. We were off by $100 billion. You'll see a plugged number in those financial statements. There is an unreconciled difference number of $12 billion in those financial statements. There is an article available outside that I wrote along with Hal Steinberg, which summarized the statements and described this process. As we were preparing the statements, we tried to identify the transactions we had with ourselves. The debits didn't equal the credits and we were off by $100 billion. We were able to get that unreconciled difference down to $12 billion. But let me tell you, it could have been as high as $112 billion or $212 billion, and that is one of the biggest things scaring the people left there to prepare this year's financial statements. They have no idea what that unreconciled difference is going to be.

Since this first effort, the Federal government has implemented a process whereby agencies, when they engage in transactions with other Federal agencies, need to identify the agency. There is a code that has been added to the standard general ledger which is G or N. G meaning dealing with another government entity and N dealing with a non-government entity. If there is a G associated with the transaction, you need to have an agency code associated with the transaction. The idea is that you can identify that the transaction is with another Federal agency, and be able to determine the amount of the transaction. When we pull it all together at the government-wide level, we can make the necessary eliminations. This elimination of intergovernmental transactions is one of the biggest problems that has to be overcome before the Federal government is able to get a clean opinion on its financial statements.

Another one of the issues that is creating a bit of a problem, is the reconciliation of the change in net position and the budget deficit. In the Federal government, the most widely publicized figure that we have is the budget deficit. The budget deficit is the thing everybody waits for in early October to see what the deficit was in the year that just ended. For years, we had deficits in the $200 billions. Last year we had an $80 billion surplus, and everybody thought it was the greatest thing since sliced bread. The problem is that budget deficit and surplus is calculated on a cash basis. These financial statements are prepared on the accrual basis. The consolidated financial statements of the Federal government are prepared on the accrual basis. We need to do a reconciliation of that cash basis deficit and the accrual basis, change in net position.

We do not have the underlying data available to do that reconciliation. It requires some analysis of the individual agency accounts. That information just isn't readily available. It will be available at some point in the future. The General Accounting Office raised that as one their issues in connection with the financial statements this year, i.e., the fact that we weren't able to reconcile. We reconciled, but basically we plugged. We said there were timing differences in the recognition of revenues and it was this number, and timing differences in the recognition of expenses and it was this number. Who knows what was in-between those buckets. That's something that we need to refine.

Here in the United States, State and local governments have the same problem. But the State and local governments do reconcile the budgetary basis financial statements and the accrual basis financial statements. We need to do the same thing in the Federal government. That's what the GAO is highlighting in their report. Those are some of the unique things that we had to deal with in the preparation process.

Going over some of the highlights of the statements, the first thing I want to go through rather quickly is, as I just said, the basis of accounting. The financial statements were prepared and presented using the accrual basis. The accrual basis means you recognize revenue when you earn it, expenses when you incur them, as opposed to the cash basis, where you don't recognize revenue until you collect it or expenses until you pay them. The financial statements were prepared on the accrual basis. That's one of the highlights. That's all explained in the management discussion and analysis and the summary of significant accounting policies.

If you look in the statements you have in front of you, you'll see the management discussion and analysis. In future years, the objective is to put the Federal government's performance measures and performance goals in that MD&A. In the United States right now, a lot of attention is being paid to performance measurement. There is a law called the Government Performance and Results Act. It requires agencies to develop strategic plans and performance measures for their major programs and activities. It also requires a government-wide performance plan. The objective is in future years to put those performance goals and objectives of the Federal government in the financial statements as part of the MD&A. Who knows if we'll ever get there, but that's one of the goals.

In terms of other highlights, in the Federal government we follow accounting standards that have been designed specifically for the Federal government. So this term, net cost, is a term used in connection with those accounting standards. Basically, net cost is the difference between your full gross cost less the revenue you earned associated with those costs. The idea of getting down to a net cost number is to show the amount that is left that has to be financed through the taxation process. So we take gross cost and we subtract from gross cost the revenue we earn from providing those goods and services. The Federal government does have some revenue. We earn revenue for allowing people to use our grazing lands. We earn revenue for allowing people to use the parks. We charge fees for certain things. All of that is considered exchange revenue, leaving you net cost. Net cost is the amount of cost then that is left to be funded through the government raising revenue through its sovereign power to tax.

What we ended up with in the Federal government is gross costs of $1,700 billion, almost $1,800 billion. These numbers are beyond belief. We're looking at $1.8 trillion of gross costs. We have exchange revenue of $158 billion, and we had net cost of $1.6 trillion. The biggest component of the Federal government's cost was the expenditures for human resources. They were about $933 billion. Human resources consists of expenditures on health, Medicare, education, Social Security and veterans' benefits. Our second biggest expense was interest. That was $246 billion. Our third biggest expense was national defense, $233 billion. You would see similar numbers in the budget. The budget would show similar numbers as these because there isn't enough of a difference on the expense side between cash and accrual. Once you get over the initial first year of recording the accrual, where you see the big thunder boomers is on the liability side. I'm going to move past the assets and move to liabilities and commitments.

These are the numbers that nobody ever saw before because we never reported liabilities in our budget, because we don't budget on the accrual basis.

The Federal government as a whole had liabilities of $6.6 trillion. The largest is represented by Federal debt securities. That was $3.7 trillion. The Federal government's debt is $3.7 trillion. That $3.7 trillion does not include the Federal securities held by Federal trust funds, e.g. Social Security trust fund, Civil Service Retirement trust fund, and some of the other big trust funds. That's not in that $3.7 trillion. The reason that's not in there is those amounts were eliminated in consolidation because if it's a liability on the part of the Treasury for the security, it's also an asset on the books of the trust fund. This $3.7 trillion of debt is only that which is owed to the public.

The next biggest liability was our liability for pensions, health care and other retirement liabilities. That was $2.2 trillion. That's never been seen before. What that means is future tax revenues, to the tune of $2.2 trillion, are going to be needed to satisfy that liability.

We have huge environmental liabilities. We only reflected $212 billion on these financial statements for environmental liabilities. Environmental liabilities relate to the cost associated with cleaning up Federal land due to environmental damage done to that land for whatever reason. This $212 billion for environmental liabilities doesn't include any of the Department of Defense's liabilities, because they haven't gotten around to identifying them yet. It's only the Department of Energy. That number could be five times higher. The problem with these environmental liabilities, though, is the estimating process is like hitting a moving target. Each year you estimate the cost associated with cleaning it up. The technology is moving so quickly that in some cases technology will make great leaps, and the cost becomes substantially less. This number is a floating number. It will be interesting to track the movement of that number. It was $212 billion in 1997. It will be interesting to see what it is in 1998.

Another big number, not a liability, is future commitments. The Federal government guarantees loans to all kinds of different citizen groups. It provides insurance for deposits and things of that nature. These guarantees and commitments were substantial. Our loan guarantees are $2.7 trillion. That doesn't mean the Federal government is going to be on the hook for all that. That's a worse case scenario. If everybody defaulted and we didn't raise any money by selling the assets, we'd end up paying $2.7 trillion in loan guarantees.

The biggest gorilla, the biggest item that's not on the statements is Social Security. The cost associated with future Social Security and Medicare benefits is not reflected on the financial statements. The reason it's not reflected is under existing Federal accounting standards, that's not a liability. Just to give you a sense of what that number might be if it were there, Medicare is the health insurance program that is administered by the Department of Health and Human Services. The present value of actuarial expenditures of the trust fund will exceed the present value of actuarial contributions by $1.8 trillion by 2020. In other words, the actuarial estimates of revenues and expenses projected out to 2020 show that our costs are going to be $1.8 trillion more than our revenue.

The Social Security number is somewhere around $7 trillion if you used a closed group. I don't want to get into an explanation of a closed group; it would take me until 6:00 to explain that. The bottom line here is we have huge liabilities that have never before been recognized. This isn't intended to scare anybody, but this is intended to shine the light on what the costs are with respect to the different pieces of legislation that are passed by the Congress. Now that long-term information is beginning to be shown (i.e., accrued costs), it might make the political leadership act with a little more fiscal discipline than it has in the past.

Finally, what are the benefits of these statements? If it's not clear to you by now, let me make it clear. It provides a financial perspective not previously available. We're starting to shed light on how much it really costs for our programs. The statements are also stimulating improvements in financial management. One of the objectives of this whole exercise, one of the goals, one of the benefits, is to force people to account for things properly and have it audited by an independent third party. You start getting accurate numbers.

I'll never forget a story I heard at OMB when I first started there. We were asking for some information from the Department of Defense. We were asking for some cost numbers. I asked this person at DOD how much it cost to produce this particular weapons system. The response I got was, Who wants to know? That tells you how accurate their numbers are. Depending on the audience, they give you a different number. That's no way to run a railroad. We wanted to stimulate improvements in financial management.

Finally, we wanted to demonstrate accountability. If you want to pass laws and regulations and have huge costs, fine, that's your choice. At least let the people that are electing you know how much it costs for those laws and regulations.

Those are what we see as the benefits of this statement. With that, thank you for your attention. I'll be happy to answer any questions.

MR. DYE (Canada): I had the pleasure of putting together the financial statements for the United States in 1985. When I calculated your national debt at the time it was $5 trillion, but your Congress was passing a bill increasing the debt limits from $2.5 to $3 trillion. I was intrigued since it's the first time I've seen the statements and wondered how you handled your military platforms. It looked like they were in fixed assets. We didn't do that in 1985, and there was no way we could get our hands on the inventory for the rockets and bullets. How did you handle that one?

MR. LONGO: The Defense Department gave us a number and we dropped the number into the statements. What is going to happen starting with the '98 statements? Remember I pointed out the stewardship section of the financial statement? Well, what the FASAB has done within the property plant and equipment standard and the stewardship standard is they have created a category called National Defense, Property, Plant and Equipment. This category basically deals with the Defense Department's rockets, planes and ships. Within this category, the conclusion that FASAB came to was that the important information with respect to National Defense PP&E is its condition and its existence. In other words, you want to know that the items exist and you want to know that the items are in condition to operate if needed.

Frankly, the value for purposes of historical cost reporting and depreciating that cost is really not an important issue. What is maybe more important, and this is still being debated, is comparing the projected cost of a particular weapons system to its actual cost. That may be more important. The point is that starting with 1998 financial statements, those dollars, about $800 billion of the $1 trillion are going to be dropped from the balance sheet. Information about the quantities and condition of these weapons systems are going to be reported in the stewardship section. There is going to be a requirement that you have an inventory of quantities and a condition assessment.

MR. DYE (Canada): It's a good way of handling it. The other thing that interested me, and I haven't figured it out, is how you handled sovereign debt. Did you provide for any discount of uncollectible loans from other countries? The best I could identify was something called Other Loans there. I was just wondering if you dealt with valuation of sovereign loans.

MR. LONGO: That's an interesting question. The number is not material on the government-wide statement. As a result of the number not being material, there was a huge debate. There was one camp that wanted to state the value of the loans and set up a true allowance to offset the fact that about 95 percent of it is probably not collectable. There was another camp that said, We can't do that. If we set up an allowance, we'll be sending a message to these other countries that we're not interested in collecting the debt. We would lose leverage in international economic negotiations. Because the number was immaterial to the government-wide financial statement, we finessed it by not showing anything. We did that with the concurrence of GAO. That is an interesting question because our feeling was we should show the gross amount, show the allowance. We're not giving you a breakdown that it's England, France, Germany, whoever; we're just giving you gross and net amounts. You're really not losing any leverage. But the international economists and the international financial people didn't want to show anything. That's how we dealt with it. Heck, we have debt on the books that goes back to before 1900 from countries that don't even exist anymore. We're carrying it as receivables. That's the truth. The countries don't even exist anymore. Any other questions?

MR. DYE (Canada): I can't miss the opportunity. When you were talking about the $12 billion unreconciled difference I was worried, but that too is obviously immaterial. As I recall, Secretary Rubin's letter presenting the statements set a goal of an unqualified opinion on the next year's statements. What do you think about that and what year do you really think that might be?

MR. LONGO: Let me tell you. Until we get those intergovernmental transactions identified and eliminated, we're not going to get an unqualified opinion. By taking the National Defense PP&E off the balance sheet, the Defense Department took a big step toward an unqualified opinion because the stewardship section doesn't get the same level of audit assurance as the rest of the financial statements. The Defense Department right now is undergoing an effort to try and identify the rest of its property, plant & equipment and put a reasonable value on it. They hope to be able to do that by 1999.

If they do that, when you look at the balance sheet, we're comfortable with the cash number; we're comfortable with the debt number; we're comfortable with the liability number for loans; and we're comfortable with the receivable number. The property plant and equipment is a problem and Defense is the big player there. But then, even after you fix that problem, this intergovernmental transaction elimination is a huge problem. I know OMB and the departments are working awfully hard to get a clean opinion by 1999. They're making a major effort. They're reporting quarterly. The agencies that are problem agencies are reporting quarterly to the President through Vice President Gore on the improvements they're making or their action plans. But frankly, I don't think we're going to get to a clean opinion for at least three to five years. I'd say early 2000's is when we're going to get a clean opinion.

MR. WESBERRY (United States): I have a comment and a quick question. The comment is your statements indicate that liabilities to Federal employees for benefit programs is $2.2 trillion and the total debt is $6.6 trillion. I'd like to turn that around. I think that the Federal employees have provided one-third of the financing that the Federal government has needed, and I'm sure that they hope that the government is going to pay them back. My question is you indicate that the budget is on the cash basis and you implied that it will probably continue that way for a while. These financial statements are on a different accounting basis. Do you perceive a time when the budget and the actual financial reporting will be on the same basis and therefore be comparable or comparable without the need for reconciliations?

MR. LONGO: I'd like to say yes. I'm going to give you a longer answer to that question than maybe you bargained for. Remember I talked about these individual appropriation accounts which are the basis for our budget? Our budget is really a collection of individual appropriation accounts. Many appropriation accounts make up a particular agency. One of the things that the Federal government is trying to do right now is bring some sense to those appropriation accounts.

Now, what OMB is trying to do, working with the agencies, is to get them to consolidate their appropriation accounts so that appropriation accounts line up with the individual programs that they're designed to fund. That's a first step. That's not as dramatic as going to accrual accounting for the budget. That's tame compared to going to accrual accounting for the budget. And we can't get that far. We can't get the Congress to combine appropriation accounts. The reaction from Congress varies. In some cases, it's, We don't want to lose the authority over that particular appropriation. But, more often than not, Congress wants to do the right thing. But they're used to doing things in the same way that it has been done in the past. In other words, bureaucracies don't change very much. The Congress is very reluctant to change this appropriation structure.

So to come up with a dramatic thought such as accrual budgeting would get nowhere. I must say though that there are small pockets of progress. For example, OMB has been pushing capital budgeting. They don't use the term capital budgeting, but they're pushing some sort of a distinction in the budget between costs associated with normal operations and those that provide long term benefits, costs associated with capital acquisitions. There are many that believe that that's the way to go, but its time hasn't come. I don't think it's going to happen any time soon.

MR. DENIS (Canada): My compliments to anybody who can know that much about the Federal government. I know people with more than 26 years that can't match you, starting with me. In about 1948 or 1949, the Atomic Energy Commission went up to Congress for its appropriation. They had several different appropriations. A number of Congressmen got very upset and said, For goodness sakes, go back and come back and tell us what the cost is going to be. Never mind this business about obligational authority. Paul Green, who was then the Controller, told the story to several people, including me, Congress opened the door and I put my big foot in and stopped it from closing. So they went back and prepared the budget on the basis of cost, leading to the obligational authority with adjustments for changes in unliquidated obligations and changes in inventories and so forth. The accounting system and the budget system were compatible. That went on for a few years.

Then the Bureau of Reclamation went up to the Congress with a cost-based budget. The chairman of the committee listened. After an hour or so, he said, Okay, go back home and come back and tell me what were your 01 obligations, and what do you expect them to be next year. That was the end of cost-based budgets as far as I know. Do you think that this type of endeavor and accomplishment, which it is, will lead to the possibility or the probability of presenting budgets on the basis of what it will cost to operate rather than just on the necessary obligational authority without backup to cost?

MR. LONGO: One of the things that the Federal Accounting Standards Advisory Board has done is pass a cost accounting standard. It requires the financial statements and the programs reflected on the financial statements to reflect the full cost of programs and activities. Remember I pointed out that we're trying to align Federal programs with the appropriation accounts that fund those programs. For those agencies where we've been successful, our expectation is you're going to see a financial statement with full cost and a budget account and an appropriation account for the same program, and that cost is going to be substantially less. Hopefully that will be a driver for the Congress to say, Wait a minute. Why are you giving me two different sets of numbers for the same program? Why isn't the budget number reflecting the same as the financial statement, or vice versa? That's our hook. I can't tell you it's going to happen.

MR. DENIS (Canada): One last comment. NASA went up in the early 1960s with a cost-based budget because somebody required it, and got the same answer from the Congressman who was chairman of the committee. Okay, that's great. Now go back home and give it to us on the old basis.

MR. LONGO: You mentioned NASA. NASA was one of the agencies that was very successful with this budget go-around in terms of reallocating their budget to align programs with appropriation accounts, and then reflect the full cost of those programs. They met with a great deal of support on the Hill. There are pockets of legislators who recognize the benefit and the importance of full cost. But it's a hit and miss kind of thing. You hit one committee and they're for it. You hit another committee and they're against it. It's not something universal.

MR. EINHORN (United States): It's encouraging. I'm glad to hear that some of the NASA seeds are taking root. Thank you. My compliments.

A Special Preview of the Future of Financial Management in the New City/State The District of Columbia: An Overview

Dr. Abdusalam Omer, Deputy Chief Financial Officer for the Budget
The District of Columbia

Good morning, ladies and gentlemen. My name is Abdusalam Omer. My native land is Somalia. I'm here to speak about a transformation a transformation from financial crisis to sound financial management in the District of Columbia.

I'll speak briefly about the historical background, i.e., how we got into the predicament. My colleagues on the panel will speak about what we did to get out of it, what we have to show for our efforts, and, most importantly, what the future holds for the District of Columbia.

The District of Columbia Self-Government and Governmental Reorganization Act passed in 1972. This created a Mayor-City Council form of government. However, the U.S. Congress still had final authority on District issues.

The unique structure of the District of Columbia government created unique conditions and burdens. There are property tax limitations. Because so much of the Federal government resides in the District of Columbia, 41 percent of the property is tax exempt. Commercial development is constrained by building height restrictions.

While the District of Columbia does not enjoy State benefits, it is required to perform both State and local government functions.

Congress limits the ability to tax income earned in the District of Columbia. At Virginia tax rates, the District would raise $800 million a year. As it is, the District is forced to tax a smaller tax base at a higher rate.

The District of Columbia soon found itself in a financial crisis. The lack of a strong financial management infrastructure went unnoticed due to healthy revenue streams. The economic downturn revealed the dysfunctional nature of its systems. There was a serious structural imbalance between revenues and expenditures.

Things needed to be brought under control. The first action was to establish the District of Columbia Financial Responsibility and Management Assistance Authority to oversee the District's financial recovery. The District would remain under this Control Board until five consecutive balanced budgets were achieved.

The Authority also created the Chief Financial Office, and independent Chief Financial Officer, the CFO. The CFO is appointed by the Mayor, but can only be fired by the Control Board. The CFO has the legal right and exclusive authority to implement the budget, to have fund control and to disburse funds.

The National Capital Revitalization Act, passed by Congress, created a Chief Management Officer to oversee operations of major departments and functions. The Act also required the Federal government to assume responsibility for several State-like functions.

There has been a dramatic change since 1994. We are changing the culture of District employees to obey, what we call, the rule of law, to respect their budgets, and keep expenditures within their planned budgets. Nat Gandhi, on the panel today, will tell you there are people who haven't paid taxes. There was no such thing as tax administration in the District. My friend, Tom Huestis, who is here, is doing well to put the District back on good footing with Wall Street so we can borrow money for less. I only mention some of these issues. My colleagues will discuss them.

I also have with me the Controller, Tony Pampa, who, for the first time in a long time, has provided the District with a clean audit in 1997. We are also modernizing financial management in the District of Columbia. We're moving out from the dark age to the modern age. Most of you come from the cities. You come a lot more technologically advanced than the Washington, D.C. government or, for that matter, the Federal government itself.

I just wanted to give you an overview of what it is like to live in Washington, D.C. and to work for it. It is a beautiful city. It is an international city. It is a city that has a long history. For those of you who come from other places, you should go out and visit. Don't spend all of your money in Virginia. You should spend some in the District so we can collect some taxes.

Thank you very much for your patience, and after my colleagues make their remarks, maybe we will have a session to exchange views. I would like to present Tom Huestis. Tom is the Treasurer for the District. Tom is not from Somalia. He is an American, from Pittsburgh.

Financing Local Government in the 21st Century

Tom Huestis, Deputy Chief Financial Officer for Finance and Treasurer
The District of Columbia

I've been in the consulting business with municipal finance for 10 years prior to coming to the District. I was actually hired by the District to put together the financial recovery plan. So, instead of talking about what is going on in D.C. Treasury right now, I thought it might be useful to step back a couple of years ago, and talk about how we got out from where we were. What was our plan, in terms of our financial recovery to get out of the mess we were in? This will help you to better understand a lot of the things that the gentlemen here are going to talk about in terms of what they're doing now and all the great things that they've implemented and the great position that we're in right now.

A couple of key background facts: The financial recovery was accomplished primarily with financial staff. We had very little support from the executive side of government. There was a big concern on our part and from others about whether we could, in fact, turn around a local government with primarily financial people, and with a hostile executive. But, as you will see from the results that you'll see later on in the presentation, we were all very successful.

One of the reasons we were successful was because the CFO, the Office of the Chief Financial Officer, was given extraordinary powers. We were given power over all the financial functions. Financial employees report directly to the CFO. It is unusual for an organization in the United States or a municipality in the United States to have all budget, treasury, accounting systems, all tax systems, report to the head of a financial function who is independent, in many ways, from the executive. You cannot be fired by the executive in this forum. The CFO was also given at-will employment authority, so all financial personnel were made at-will; they could be fired, or they can serve at the pleasure of the CFO and his delegates. So the financial personnel in the agencies, the accounting manager in the office of the public works, the treasurer, everybody was made at-will to the CFO. The CFO was given ultimate power there.

We were in pretty bad shape about three years ago. We had lost our market access. We could not access capital in the debt markets at all. We were about 200 days behind in making all of our general payments. We had an accumulated budget deficit of negative $500 million of a $5 billion operating budget. We had so many operating deficits that we had an accumulated operating deficit of negative $500 million. Then, we had major service delivery disruptions, as Dr. Omer mentioned. The morgue lost its air conditioning and they couldn't get it fixed. There were some major, major service delivery problems, and it was felt that the city was on the verge of collapse at the time the Control Board was instituted.

I'd like to explain to you the financial recovery plan. Step 1 was to immediately implement operating procedures and changes to stabilize the District's financial position. We'll describe them in a minute, but basically it was a three-legged stool. We needed to make administrative changes immediately, we needed to put in financial controls, and we needed to provide an organizational framework to build support from our different stakeholders that would allow us to do what we needed to do.

Step 2 was to begin establishing long-range plans to act as a guide to deficit reduction. We had to get the numbers turned around. We couldn't keep sliding down in terms of a $500 million operating deficit. We had to go back up the other way, and so we immediately started a plan for what we could do in terms of long-range plans. Long-range plans for us is six months to two years. I mean, it wasn't long long-range plans, but there were some things we needed to do immediately in Step 1 and then there were longer-range plans in Step 2.

Finally, once we began making some traction in both Step 1 and Step 2, we needed to seek the Federal government's relief to fundamentally change the relationship between the District and the Federal government. The structural relationship between the Federal government and the District just didn't work in the long-term and we knew we needed to renegotiate that deal. But, the only way to do it was to make progress and to gain some credibility through Step 1 and Step 2.

The three goals of Step 1 were all interrelated. We needed to build support in the Congress, in the credit markets, and in the local media and populous. We also needed administrative changes. We needed very much to change the personnel that was there, the organization, and the corporate culture. Then we needed to gain control of the ultimate financial transactions that were happening day-to-day, and those are the basic fundamentals for a financial organization which is cash. We needed to control cash cash coming in, cash going out. Accounting for cash was the basis for survival of our organization.

In the administrative changes that we made, we replaced all major heads of all the financial functions. We are all the benefactors of that here. We are all the replacements. Our former boss replaced all the major heads of the financial organizations. We reorganized some financial units to meet the short-term goals, particularly in terms of building support in the Congress, the media and public. We changed the organization in order to make sure we were building that support. We relieved more than 200 personnel of their jobs. There was a major change in terms of the personnel. We used the personnel authority with which we had been empowered immediately after we reviewed all the financial personnel that were under us. We made changes immediately to change the corporate culture and change the direction under which we were operating. We used financial consultants to augment the staff, since we were replacing heads of organizations and since we were making major changes in personnel. We hired the consultants to augment what we were doing, because there was a list of twenty critical things for each of us. With the staff we had and the time that we had every day, we could not complete them. So we used the consultants to help us jump start the process in a lot of these critical projects that you'll hear about from my colleagues. As I mentioned before, not only did we review the personnel and dismiss more employees, but we also replaced agency personnel. Our personnel authority not only related to the core financial functions budget, treasury, tax it also reached all the financial people out in the agencies, out in the service-delivery areas. We had to change that culture too. They, too, had to buy into the system.

You can see that building support was one of the key things for us. In order for us to be effective, we knew we had major stakeholders all around. We had to gain their support to go out and do what we needed to do. If we wanted to be back in the credit markets, we had to regain the confidence of the credit markets. We did not have that confidence, so we set up an investor relations group to do that, and I'll talk about that in a second. We needed the confidence of the residents, voters and customers, the taxpaying customers, and the vendors who we hadn't paid in 200 days. We needed to regain their confidence so we set up resources and organizations to do that. We needed the media support because we would be making unpopular decisions in the next couple of years, and we needed to gain some political capital in order for us to make some hits later on in the tough decisions we needed to make. Finally, we needed the support of some of the governing bodies. Ultimately, we serve at the pleasure of Congress. Congress created the Office of the Chief Financial Officer, and we needed to have and hold their support. We changed our organization in order to do that, and the Control Board, their agency, as well.

Looking at the organizational groups we established inside the financial operations of the District, you wouldn't think of these groups as part of a normal financial organization. But they were absolutely critical in terms of allowing us to do what we needed to do. We established a media relations group that dealt with the press every day. We had three briefings a week for the press to tell them what we were doing, and we told them how bad it was. We were not shy at all. Before, everything was kept under a vest. And here we were telling them how bad it was. People knew it was bad. All we could say was, Here it is. By telling them how bad it was and telling them the steps that we were going to take to make it better, we gained the trust of the media. Then, 90 percent of the articles turned out positive. It was a very smart thing to do, and it was one that served us well.

We also established an intergovernmental relations group. We established a vendor center, a center just to deal with the vendors that we hadn't paid in years. We established a tax customer service center, which Nat will talk about in terms of the changes that he made on the tax side. We also made presentations to more than 100 community groups. We actually went out to the local community groups and told them what our plan was, what our process was, and how we wanted to change the direction of the government. We had a moratorium on complaining because if we wanted to get the support of Congress, if we wanted to get the support of the Control Board and some of the others, we couldn't just keep blaming the problems on other people or other things. We had to show that we were going to use all the resources we had to dig out and fix what we could, and then we were going to get their support, but only then. So we had a moratorium on complaining.

We had a terrible investor relationship with the credit markets. The fact that we didn't have market access says that, but it was much deeper than that. We had embarrassed people. We had not been truthful to people. We had surprised people. And, for a lot of reasons, we didn't have any trust in the credit markets at all. So we established an investor relations program in my office to rebuild the confidence of the credit markets to allow us to ultimately enter the market and satisfy our cash needs.

We set up a system right in the middle of regular communication. Every two weeks we called all the rating agencies and told them exactly what was going on, and we used the same philosophy as we were using with the media. We're going to tell them everything. We're going to show all the dirty laundry. The only thing they can learn is that we're in trouble, that we're in financial crisis, and they already know that. So, we were going to tell them everything we knew, and, hopefully, they were going to start to believe in us. We were going to be extraordinarily open. We were never going to surprise them.

We were going to understand the analyst's position. I think this is something important for you all too, as you think about how you have relationships with the credit markets. You have to understand what your analyst's position is. He or she is in a position of the company. He or she has certain needs, and he or she never wants to be surprised. If you surprise the analyst with information on the front page of the *Washington Post* before he or she knows about it, his or her boss is going to think that his or her employee doesn't know what's going on in Washington, D.C. So we were very conscious of the individual analyst's position in the company, not to build on the individual's ego but build on what was needed in terms of his or her position. We were consistent. We gave the same messages. Constantly we told what our plan was Step 1, Step 2 and Step 3. We also reached out to the ultimate purchasers of our bonds. A lot of the time, in the credit market, you're talking to middlemen that write publications and send messages and do rating. Ultimately, you also want to reach out to the purchasers of your debt. We had a plan to do that as well.

The next step beyond building relationships and administrative changes was the down-and-dirty financial controls. This is what we set out to do. We had to get control of the cash. We had to prove that we could be an ongoing organization. In order to do that, we had to control cash. Since we had an ultimate cumulated deficit, we had more current liabilities than current assets, so we had to get into the market to borrow. There was no way around it. We had to regain market access. The only way we could really regain market access was to get control of our spending and account for the cash that was coming in and going out. In the near term there were no collection efforts that were going to make that much of a difference in order to gain market access. So we concentrated on controlling spending and knowing and detailing and analyzing what was going in and what was going out. We wanted to prove to the markets that when we borrowed money we had the resources to pay them back.

In order to establish spending controls, we instituted what Dr. Omer established, as the Budget Director, a Budget Rule of Law. The District agencies had a philosophy that they had a divine right to spend regardless of what the budget was. We said, The budget is the budget. You will not exceed your budget or there will be consequences. The consequences we took were personnel actions, whereby we fired people that would not live within the budget rule of law. We could allocate spending authority. We actually allocated or incrementally gave out spending authority to agencies, usually on a quarter basis. We could also turn off the spigot in terms of personnel funding. So, if an agency refused to live under the law, we had the authority to withhold salary checks for its personnel. Once that was threatened, everyone got in line.

There were no more unauthorized expenditures. Again, in the past, the budget was not enforced at all, and legal expenditures were not enforced. So agencies had a history of making unauthorized expenditures from the budget. That was eliminated. We established a regular monthly monitoring process. Prior to this, they'd go to the end of the year, look back and say, Oh my God! Look! We overspent $100 million in our Health Department! We knew, if we were going to establish budgets, rules or parameters, that no one could be allowed to go around them. We had to make sure that there was a regular monitoring program to give us the heads up if someone got ahead of their budget. Then we could take the actions that we needed in order to put them back in the right box.

We also had to identify, organize and prioritize all disbursements. The District had never done that, and that was part of our cash accounting changes too. We needed to prioritize what had to go out in order to make sure the most critical items court orders, things that we were getting penalties on, payments, fines were paid, so that we could minimize some of our spending. Ultimately we had to identify the spending level that would allow us to repay our market borrowing. If we needed to borrow cash in the market to stay liquid, we needed to identify the spending limit that would allow us to repay all of our obligations.

Market access was defined in terms of what we needed to do in order to borrow. We needed to maintain our conservative assumptions. We had to estimate revenue low and expenditures high, demonstrate that we could repay, demonstrate our financial controls, demonstrate that we would use our controls and had the will to use our controls, and demonstrate how the cash flow works, so that they could be guaranteed repayment. Ultimately, we got back into the market and were able to borrow and stay liquid. That was all Step 1.

Step 2 was to implement long-range plans for the District, the financial plan and budget, a four-year financial plan and annual budget, including all funds, capital and operating. We had to improve the revenue and cash collection. We had to make accounting improvements and financial system improvements.

At this point, I want to turn it over to Nat Gandhi, who is going to go through the improvements and the status of where we are in terms of our tax collection efforts.

Taxing Local Government in the 21st Century

Natwar M. Gandhi, Deputy Chief Financial Officer for Tax and Revenue
The District of Columbia

As Tom pointed out, a fundamental problem here was the declining revenues in response to requests for tax payment. Basically, our tax system was broken. The major elements of the broken system was variable voluntary compliance, lack of technology and little resources.

As perhaps you know, the Internal Revenue Service (IRS), the Federal tax collection agency, is perhaps the most effective tax collection agency in the world. The heart of its success is voluntary compliance, meaning that every taxpayer puts together his or her annual income statement in a tax return, provides a voluntary calculation of taxes and sends a check to the IRS for taxes due or receives a refund from the IRS when appropriate.

Once people found out that the District's tax administration was not effective or was not aggressive at collecting taxes, they started delaying their tax payments and, in many cases, not even filing the tax returns. So, as the voluntary compliance lessened, the District made an attempt to enforce the tax laws, but because the system was broken, its efforts became arbitrary. Additionally, our senior managers were leaving the Office of Tax and Revenue at a high rate.

The Office of Tax and Revenue had 11 directors in about 15 years, so there was considerable turnover at the top in terms of providing guidance to the staff. The staff itself was highly demoralized and was not well trained. Worst of all, we just did not have the computer systems worthy of a modern tax administration. Over the last 20 years, the state and local tax administrations have gone through a technological revolution in this country, but it simply bypassed the District. Our computer system, as I pointed out, was poorly organized. We had 46 separate kinds of PC applications and we had stovepipe information systems that did not talk with each other. Not only was our tax structure broken, but, to complicate matters further, the District has 23 different kinds of taxes. As Dr. Omer pointed out, we are rather a unique administration, a unique municipality, not a city, not a state, so we have to have all kinds of taxes to supplement our revenue efforts.

To revitalize our revenue administration, the first thing we did was to hire an experienced management team. We hired all of our senior managers roughly over the last 18 months. They came from state tax administrations, from other states like Maryland, Virginia, New York and Vermont. We also hired experienced tax professionals from the Internal Revenue Service. We also trained our employees to let them know how to collect taxes, talk with customers and audit the right returns.

Then, we started to build a basic infrastructure. Most of our contacts with taxpayers is through the telephone system. Our telephone system was in very poor shape. We still had rotary telephones. So, we established a new telephone system. We also obtained personal computers and made sure that everyone in the tax office had a computer on his or her desk. Then, through training, we gave employees a process by which they would know how to perform their job more efficiently.

The training involved a reengineering of our business processes, and we told employees what we expected from them. We established key process goals. We knew exactly what we wanted to do to change the perception regarding tax administration.

I had audited the IRS as a member of the General Accounting Office, and one thing I knew more than anything else is that taxpayers in this country are concerned about their refunds. They do not want to wait for that refund. After all, it's their money, and they are waiting to get it back from the government. Nothing really motivates them to complain about the government more than that. So we made sure that we provided taxpayer refunds as quickly as possible so that they would know that something is working here. We told our people, Look, this is the goal. We must provide taxpayer refunds within two weeks. It used to take sometimes six or eight weeks, and sometimes even months. So, we energized our group and told them that this is what we wanted to do. There were three goals. We want to pay our taxpayer refunds within a matter of two weeks; decrease wait time on the telephone to no more than one minute; and deposit all the checks that come to us within the same day 24 hours. If the check came in today, it went to the bank today, a concept we refer to as zero-day deposit.

This is what we accomplished through our specified goals. As Tom mentioned, we had to emphasize the collection of accounts receivables. We explained to our people that the way to manage accounts receivable is to establish a threshold. You cannot simply go first in, first out. What we suggested to them is to identify which of the receivables are more important, which are high-dollar amounts. Let's concentrate on all the tax debts more than $2,000. By managing our accounts receivable, we were able to collect $52 million more than was collected in 1996. So, it was a 100 percent improvement in 1998. Refunds were provided in 15 days rather than the usual 60 or more days. By improving our processing, we were also able to reduce errors generated through returns processing. And that improved over all accounts. Lastly, we deposited the checks that came in within a matter of 24 hours, and we deposited close to $300 million on a zero-day deposit. That really stabilized incoming revenues and customer services. It also had a profound impact on the populous at large. The public, for the first time in a long time, felt that something was working. By concentrating and focusing on a very few things, we were able to tell them that these are the things we can do and we will do.

In 1998, and further on into 1999, one thing is fundamentally clear we are not going to lose the ground that we gained in 1997 and in 1998. We are going to be absolutely sure that we keep collecting cash by aggressively pursuing accounts receivable. We are going to be absolutely sure that our accounts remain clean, without errors. We will process the returns without errors so that we will be able to get a clean and unqualified opinion from our external auditors. And, of course, and we want to be absolutely sure that we keep on depositing the checks properly.

To do all that, we established a customer service organization with telephone units for audit and collection, and we started an administrative appeal procedure within our own shop. By telling taxpayers that they have a right to appeal, they really don't have to take our word for it. They can appeal, within our own office on an independent basis, so that they have due process. We also established an internal audit and security division within the tax office to assure that our own people are up to par, and full of accountability and financial integrity.

As Dr. Omer pointed out, our problems here are far greater than simply a poor tax administration. We can improve our tax administration, as we have done, but our fundamental problem relates to that unique nature of the District, which is not a city, which is not a state. Our tax base is quite limited as, again, Dr. Omer pointed out. The District does not have the capability to tax all income generated with the city. For example, if a person lives in Arlington, Virginia, but works in the District, Virginia benefits from the revenue generated from that person's income tax not the District of Columbia. This is the only jurisdiction in this country that does not have the capability to tax all income that is earned within its boundaries. We cannot tax the Federal operations that have economic enterprises here. As Dr. Omer pointed out, 41 percent of our real property is in tax exempt areas, either Federal government, diplomatic institutions, churches and universities. That is a very large amount of real property that is tax exempt. We also have a unique problem with our height limitations. Any buildings above certain heights cannot be allowed in the city, primarily because they want to maintain the architectural structure of the city.

Because of this limitation, our financial house, our tax structure, is rather cumbersome. We have five different kinds of property taxes. We have professional license fees. We have another 100 fees that are very difficult to administer, and our sales tax structure and other taxes are so cumbersome that administratively it is extremely difficult to carry on a legitimate tax policy.

To summarize, our current tax policy is complex, it is difficult to administer, it results in tax evasion, and it is exacerbated by cumbersome administration methods which, above all, discourage voluntary compliance.

So, our Chief Financial Officer has given us a vision. What kind of tax policy, tax structure, should you have in the city? What we really want is a tax policy that would be far more competitive with surrounding jurisdictions. For example, we are currently in Virginia. Virginia's taxes are about 60-70 percent lower for the business taxpayer than they are in the city itself. It is the same with Maryland. We want to make sure that our tax system is simple, fair, equitable and administrable, and that we make sure that the customer is served. Lastly, we want to maintain our revenue structure that is, the cash coming in should be properly protected.

By improving tax administration, we were able to stabilize our revenue base. But that is not enough. We need to think in terms of improving our tax systems, bringing them up to the 21st century. We still do not have integrated tax systems. We are still somewhere in the 1960s and 1970s in terms of our technology. To provide a first-rate tax service to our customers, to assure a stable revenue base, to close the tax gap that exists currently in the city, we need an integrated tax system where all different kinds of taxes talk to each other. That is the fundamental problem that the Internal Revenue Service has at the Federal level, and what we have at the state and local level. That is where we are going next, and LaMont Wells will talk about how we are going to think in terms of making sure that technology will help improve our tax administration. Thank you.

Improving Local Government Financial Information in the 21st Century

Anthony Pompa, Deputy Chief Financial Officer for Financial Systems and Controller, The District of Columbia

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My name is Tony Pompa, and my office is the Office of Financial Operations and Systems the accounting office. As my good friends remind me all too often, I probably have the least exciting job of all of us. But, my job is equally important to our collective mission, and that is sound financial management of the District. As Dr. Omer told you, in 1994 the District was in very bad fiscal condition. The financial condition of the District could not get any worse. To compound that, the accounting office could not present to its stakeholders what the financial position was.

Our number one responsibility is to prepare the comprehensive annual financial report. That tells our stakeholders the citizens, our governing bodies and our investors what our position is. If that is inaccurate, as attested to by the independent auditors, then these stakeholders cannot make sound financial decisions. Our then Chief Financial Officer made it the collective goal of our organization to obtain an unqualified opinion, or a clean opinion, on the 1997 comprehensive annual financial report. Many of these changes that my colleagues have talked about have started to yield benefits. Who would believe it, or who would know it, if we could not present it in our annual report and have it be certified as accurate? We went from a $74 million deficit in 1996 to a $185 million surplus in 1997. But, if we did not get a clean opinion on that report, who would believe it? And who would believe the improvements we were making? This wasn't an easy task.

There were many obstacles that we confronted to get this clean opinion. We had an outdated financial management system, and Mr. Wells will tell you about the new system we've just installed, but the old one was 20 years old. In America, especially the District, that is extremely outdated. Associated with this old system, we had a cumbersome, time-consuming, manually intensive closing process, and there were many broken business processes that had to be changed. As Tom told you, there was a large-scale dismissal of employees to change the culture of the workforce. But with that dismissal went some of the know-how. So we were confronted with people who were inexperienced in this closing process. Then, we didn't have a plan, strategy, or an organized approach to how we were going to achieve our goal.

The plan was quite simple. It wasn't any sophisticated strategy that we developed. We created a clean audit goal committee. We conducted a lessons-learned study what did we learn from the previous close? We did a vulnerability assessment from a financial reporting perspective, where were we weakest? We established a policy and procedures unit within our office, as well as an internal control or internal audit unit. We focused on fixed assets, and we provided some training. I'll speak briefly about each of these steps.

First, let's discuss the clean audit goal committee. This was comprised of members of my offices and agency financial offices. We developed a monitoring system. In conjunction with the 1996 qualified opinion, the auditors gave us a management letter report on internal control weaknesses that was thicker than a District phone book. There were hundreds of comments on deficiencies in the financial management function. We assisted agencies in developing action plans to eliminate these comments and weaknesses. We then tracked the progress of these plans. So, we knew, on a weekly basis, if these deficiencies were being addressed.

The second part of the strategy was lessons learned. We engaged the services of a public accounting firm to perform an assessment of the closing period that was just completed. We wanted to identify the major hurdles that we had to get over so as not to repeat them. We refined the closing process. This closing process was associated with our 20-year-old system, so we streamlined the best we could, we consolidated some functions, and we automated some tasks.

The next strategic point or action we took was a vulnerability and at-risk assessment. In this case, we also engaged the services of a public accounting consulting firm to perform a citywide vulnerability assessment and identify high-risk areas. The area that caused us to receive a qualified opinion in 1996 was our tax receivable number. We knew that there were more problems in the tax area, and we wanted to address these problem areas before they became what we'll refer to as qualifiers or showstoppers.

The next action we took was creating, within my office, a policies and procedures unit. Many of the management letter comments and internal control deficiencies would be or could be corrected or eliminated if we would only have citywide policies and procedures for people to follow. What this unit did was draft and publish citywide accounting policies, and they coordinated the documentation of desk procedures within all of our offices. We knew how to get from the beginning to the end. Up until this time, nothing was recorded on how to do things.

In conjunction with establishing a policies and procedures unit, we established an internal control unit. The task of these unit members is what the title suggests. They would verify that financial personnel would conform to these policies and procedures that were developed and promulgated. They would also assist the consultants in identifying at-risk areas.

One of the problem areas identified was fixed assets primarily accounting for our personal property. Our own vulnerability assessment and that of the hired consultant indicated that over the past several years, 70 percent of governments or entities that received qualifications on their annual financial reports did so in the fixed assets area. So, we established a fixed asset committee and, again, we contracted the services of an asset management firm to take physical inventories. We then reconciled actual counts to what we had booked.

Finally, the last step, and maybe the most important step, was providing training and closing assistance. We brought the agency accounting people into our office and made sure they knew how to get the job done, how to close the books and how to record activity correctly. We again contracted a public accounting firm to assist us in this area. You may have noticed there was a prevailing theme. We had to go out and hire help in most of these steps. I am pleased to say that we will not have to repeat that this year and in the ensuing years for a couple of reasons. One, we've learned how to do it well, and, as Mr. Wells will tell you, we're implementing new systems which reduce the amount of manual intervention required to perform our task.

With that, I'd like to introduce Mr. Wells, our Chief Information Officer. He's going to tell you about all the new and exciting things we're going to do in the next century.

Information Technology for Local Government in the 21st Century

LaMont Wells, Chief Information Officer, The District of Columbia

I am LaMont Wells, and I am responsible for bringing together, in a technological sense, all of these programs and agencies that have come before me. The difficulty of my task, obviously, is that the architecture we started within the District was nonexistent. We had antiquated systems. They were archaic to say the least. The information systems we had were dumb terminals, 286 and 386 computers, and, in most cases, nothing at all. We have moved from training people on how to operate the mouse on a computer to the evolution of implementing major information systems. I don't think it is important today to talk about the architecture in a technological sense. It is more critical that we talk about the strategy we employ to ensure that we can achieve the vision of the Chief Financial Officer, i.e., an integrated financial operation system for the District of Columbia.

Our mission in that regard is to take a look at innovative information technology. To build a world-class financial operation supported by information technology, we have to be sure we understand and we recognize that there is a synergistic relationship between the business operations of an entity and, of course, the information technology which is an enabler to ensure that we can do those things that we need to do.

Our challenge in that regard, as we take a look at the old model we found in the District, is that we have nonstandard systems. The architecture is in fact not standardized at all. I've gone over with you in a little detail the challenges we had with respect to just training people how to use desktop applications and PCs, but more importantly we did not have an information technology strategy which would support the vision of the corporate executive, in this case the Chief Financial Officer. We had projects that were decentralized, stove-pipe applications that ran through all of our agencies that had no connectivity, and no integration. More importantly, we were faced with the challenge of implementing three major corporate information systems, all in the course of a two-to-three year period of time. In addition we were facing the Year 2000 challenge, and the requirement to ensure that we would have a clean opinion. So the issue was how do we get from that old model to a new model where we do in fact have centralized technology, where we do have an architecture that is standardized, where we can in fact treat our projects like an investment portfolio, and where we can overcome this beast called Y2K (Year 2000) in addition to maintaining day-to-day business operations?

We developed, in that regard, core values, and we understand that these core values are really linked to the business of the day for us. That is the recognition that information technology must be inextricably linked to the organization's business strategies. We also take a look at that synergistic link with the corporate vision, and that is the integration of our program and our financial operations. Then, we have to understand that in order for us to be of any assistance, we must add value to the corporation's overall goals and its objectives.

I'd like to discuss our priorities, and one of the first is to remediate our Y2K exposure. We have old systems that are 1970s and 1980s vintage. We have people who have not been trained since the

1980s, and we're trying to overcome that. In the midst of that, we are trying to take old code, remediate it at the same time and, in a parallel effort, we're implementing new corporate information systems. The implementation of these systems will help us to alleviate some of the remediation challenges that we have but, to be sure, we'll not resolve all of our problems. We still have quite a few stove-pipe operations that Nat talked about earlier throughout the applications that we had to develop in order to do business on a day-to-day basis.

If we do these things, we have to do them concurrently, and we recognize that it is a great challenge for us. It is a daunting task because we don't have the skill sets and we are under-resourced. We are under-trained, and we are undermanned in a lot of the critical information technology skill sets that we need to do our job.

So, our challenge is a challenge you can see not only in government, but also in the corporate sector. You'll see that it is very difficult for not only the District, but also the private and other public sector venues to recruit, to retain and to train and hire skilled information technology personnel. That is a major challenge for us. If you can get a visual picture of where the District stands with respect to the other presenters this morning, you can clearly understand our challenge in attracting information technology skilled sets to the District to help us resolve our problems. That, in and of itself, remains our number one challenge as you see the model across the country. But yet, in addition to that, Y2K is always looming on the surface.

So we set up a technology framework that allows us to look at three tiers. The first is to add visionary leadership, and that is to provide an information technology strategy that will embrace the business operations of the Chief Financial Officer's Office.

The second tier is to develop an organizational structure by establishing the role of a CIO or a director or deputy for information systems. This was not done heretofore. We did not recognize, 18 months ago, that we needed to have information technology as an enabler. So we are building a new organization. We're redefining the roles of the chief person that is responsible for information technology and operations within our department. In addition to this, we are trying to staff and train our people so that we can accommodate the challenge before us.

The last tier is the empowerment of project integration, and that is recognizing that these projects which are over $120 million in capital funding are in fact a capital investment in our future. Here, we can take a look at where we stand with respect to that and we see that we do a very good job in terms of planning, and a poor job in terms of execution, based upon the construct that we had in the past. What we have is a technology gap in the District, a communications gap, where we have skill sets that are isolated. We have knowledge centers, but yet we have people who are not confident and comfortable in their skill sets. Therefore, we don't have information sharing. We have organizational barriers that we must knock down. In addition to that, we have a competency gap where people have not been trained since the 1980s in terms of technology. We are reversing this so there is an understanding of the new technology. As you are well aware, technology changes almost daily. There must be an understanding of the new technology, but more importantly, there must be an understanding of the leading-edge technology embedded in the three corporate information systems that we're going to put in place.

So the challenge for us is how do you win the no-win situation? We took a look at organizational dysfunction and then we looked at those types of organizations that work in harmony, and we realized that lack of communication is perhaps 80 percent of our problem. This encompasses a lack of understanding about information technology and how it applies to the business goals and objectives of an entity. It is also the lack of understanding in terms of how we need to bring these together to bring to bear a critical mass to resolve and to solve our problems from a technology standpoint. So, I say to you, that perhaps a larger part of my challenge is the challenge of effectively communicating the top priorities within the CFO from a technological standpoint.

We look at the current model of a normal organization that takes a step and they go from noncompliant to controller compliant to leadership. We don't have the time to walk our way methodically through this model. In fact, what we have to do is go through a metamorphosis. We have to literally leap from a noncompliant model, in terms of technology, to a leadership model and really brute force this thing through in the midst of the technological metamorphosis that we're going through.

Nat Gandhi in the Office of Tax Revenue, is redesigning his entire tax administration system to ensure that we don't embed new technology on old processes. So we're looking at core competencies. We're looking at value-added competencies to determine the functions we need in a work flow so that we don't have duplication of processes or a duplication of effort. Then we streamline it and then we embed technology on top of that. We're not only doing that in the Office of Tax Revenue, but also in all of our other departments as we move through. We don't want to put good technology on top of bad processes. So, we look at the policies, we take a look at technology, and then we look at the people and how we need to train them in order to deal with the new technology we have and to be sure, on the four-legged stool, if any one of these entities is missing, then we have a totally dysfunctional operation with respect to supporting it with information technology.

So we looked at our challenges today and we look at it in a three-tiered approach. We have to take a look at Y2K and the Year 2000. We have to take a look at implementing these three corporate information systems two of them in one year and then the third one in a two to two-and-a-half year period of time. We then have to take a look at developing a standardized technology through the District's LAN and mainframe operations that allows us to effectively operate these systems.

Our critical success factors are these. We recognize that information technology is inextricably linked to fiscal integrity. I think you can get fiscal integrity, but you have a difficult time maintaining it on a year-to-year basis without a technology foundation.

To be sure, we are clearly in the business of expediting the delivery of information so that key leaders in the District have the platform that they need in order to make executive-level decisions. They have the right information, accurate information and timely information with respect to the financial, budgetary and treasury information.

We have to implement our projects, these capital projects, the integrated tax system, the system of accounting and reporting, and the comprehensive automated payroll and personnel system on time, within schedule and obviously we have to do it within cost.

In that regard, we have to treat our information technology as an enterprise. We have to turn it on its ear, so to speak. We have to be able to take it out of the old paradigm and change our corporate paradigm. We have to treat it as an enterprise. We have to develop charge-back methodologies for the use of our mainframe operation, and we have to have a return on our investment that is consistent with what it is that our bosses would need or want or desire in the implementation of these systems.

So we look at a financial systems strategy that treats our financial systems on an enterprise-wide basis with an enterprise-wide strategy. We view information technology as a tool, to ensure that the taxation, financial and budget departments can all come together in a synergistic way. In the short term, we look at the three corporate information systems that we have as the tools to do that the integrated tax system in the Office of Tax Revenue, the comprehensive automated payroll and personnel system in the Office of Financial Operation Systems, and the system of accounting and reporting also in the Office of Financial Operation Systems.

Our long-term strategy, however, is to get out of the mind set of the stove-pipe operations the same mind set that got us into trouble in the 1960s and 1970s. It will get us into trouble in the years 2000 and 2010 if we don't address it today. We can't use a stovepipe mentality, process or methodology. We have to have a way, either electronically or through some technology, that allows us to treat all of these systems as one, seamless financial management system. We're moving in the direction of putting them all in place in each of our different departments, but yet we lack the capability right now, as we are developing these systems, to ensure that they are integrated. There is some interface there, but no integration. Integration will allow us to have capabilities where data can move freely from agency to agency, department to department, at the Control Board, in Congress, or wherever that information needs to be present and available.

Our first major system under the Office of Tax Revenue, which is Dr. Gandhi's system, has three basic modules to it. It is the largest endeavor of its kind in the taxation business in this country. It has three modules a business tax module, an individual income tax module and a real property module. It is extremely large in terms of its millions of information per second and its architecture. It is a tremendous endeavor. It is based and predicated upon a tax administration system that is a proven technology in other jurisdictions. Our challenge, however, is that no other jurisdiction is moving in a direction to integrate all three of these modules all in one. It is a three-tiered technology that consists of a mainframe middle ware, a client server application and front-end imaging. That front-end imaging is an ICR/OCR that is imaging character read and optical character read. In addition, it has a data warehousing capability within the Office of Tax Revenue that allows Nat to go into that data warehouse to retrieve our carbodata to do economic forecasting, to do taxation forecasting, and to do revenue projections. This is the sort of information and projections he needs in order to manage his operation on a day-to-day basis.

It is also a single integrated application environment. That single integration is a proprietary data application. It maximizes the use of proprietary data of the contractor to ensure that we can take the business processes that we talked about earlier and embed state of the art technology on top of the reengineered solutions. In addition to that, it allows us to develop a software capabilities maturity model that is consistent with the standards from the General Accounting Office. This is the first time in the District that this has happened on any project of any size. This project has that embedded in it, and we think it will serve as a pilot and a model for how the District will implement information technology solutions in the future.

The comprehensive automated personnel and payroll system is an integrated management information system model that has five modules to it. I won't go over these modules in any detail, but just very quickly, the five modules are: position control, time and attendance, employee processing, benefits compensation and payroll. The key here is that this system is a system that pays people. It is the system that maintains the personnel files. It is a system that takes a look at labor distribution and how we do it. As you know, a construction worker working in the summer makes a different rate, perhaps, than in the winter, depending upon the job. This system allows us to discern those differences in labor categories as well as labor policies and labor laws, and it provides us with a state-of-the-art technology to rapidly pay and more efficiently pay people. Not only can we pay those that work in the District, but also our vendors, as it also interfaces with 70 different agencies in the District. That's not to mention the tremendous interface between it and our financial management system, the new technology that we're bringing onboard. The most important thing here is that the new system is, in fact, Y2K compliant, including the integrated tax system in the Office of Tax and Revenue.

Our next system is our SOAR (System of Accounting and Reporting) system. It is a world-class financial management system that provides accurate and timely information in these three functional areas: the budget, accounting and fixed assets and inventories modules. It is connected or interfaced with 48 different agencies, and these interfaces will increase over time. The key is that it improves performance, ease of use and customer satisfaction. It allows us to pay our vendors much more quickly and more efficiently, to receive funding into the District much more efficiently, and to give leaders a bird's-eye view, up-to-the-minute, on-line access to financial reports in the District. We no longer have to wait hours or days or weeks. It is up-to-the-minute, and it is available to every manager with this application and the workstation on his or her desk. This is a look within the District, a look that has never been presented to the District, and we hope it will serve as a model for other municipalities of similar size and scope.

These are some of the benefits of our system of accounting and reporting. We will be able to strengthen fiscal control or financial control by allowing the budgeteers and our financiers to have up-to-date information on financial reporting. We have to be able to track effectively our grants and our capital projects. In addition to that, we can record obligations, and then, of course, pay people in a timely manner, in a manner indicative of an efficiently operating government.

If we don't get past Y2K, everything else doesn't really matter. We're concerned about Y2K under three legacy systems that are being replaced by the capital projects that we just talked about. In the Office of Tax and Revenue, Nat and his staff have done wonders with respect to remediating and testing existing code that they had on the legacy systems, the business tax information system as well as the personnel and income tax systems. So we're really far ahead. The District, as a whole, is about 18 months to 24 months behind the rest of the world. However, I think in the Office of the Chief Financial Officer, because of the work of that staff, and the Office of Tax and Revenue, and the staff in Tony Pompa's office, the Office of Financial Operation Systems, we're really further ahead in terms of remediating our legacy system code than a lot of other agencies within the District. We're also remediated by the course of natural events. Nature has taken its course with respect to the implementation of new systems that come Y2K-compliant.

Our key here is that, unlike any other jurisdiction, as Drs. Omer and Gandhi have said, our oversight is horrendous and very, very tight with Congressional, City Council and Control Board interest on these systems. Because we pay U.S. Treasury, the Secret Service, judges and the Park Police their pension checks, we automatically get GAO visibility and Congressional visibility. So we put a structure in place where we do in-house remediation and we established an in-house project management office to link up to the District's Y2K project efforts, which is a management reform effort under the President's Revitalization Act.

How do we get from stove-pipe operations to one seamless financial management system? We have to use the enterprise-wide data warehousing capability, and decision support system applications, and integration of those applications to get to this model. If we look at the integrated tax system, the accounting and reporting, and payroll and personnel systems across all the agencies with which they have to interface, the question is how do we get this box read? That's our next challenge as we move forward. You'll see that in some of the initiatives that we have coming up for information technology.

Nat Gandhi is working on the modernization of the CAMA system, the computerized assisted mass appraisal, also his recorder of deeds modernization, a historical site which is also going through a major modernization effort now. He is also doing electronic tele-filing, which clearly puts the District years ahead with respect to the collection of low-level taxes. He developed a pilot over 18 months ago. It's gone beyond the pilot stage and has gone into the developmental stage, where it is being used now, We hope to expand that a little bit more.

Tom Huestis is also looking at electronic bank transfers. We are looking at developing a financial information infrastructure, an enterprise-wide solution to integrating all of the financial systems so that we get a bigger bang out of the buck and we have a critical mass with respect to the information technology. We're looking at not only Internet, we are looking at Intranet within the Office of the Chief Financial Officer. We are using Web browsing technology on our system of accounting and reporting to do remote printing and also provide access to financial reports through the Internet.

We're looking at imaging. We're taking Nat's lead in the integrated tax system, and looking at how we take 12,000 files from our pension system in a room on the third floor that is dusty, cobwebbed and probably has bats, and download that data to CD-Rom technology. And then apply a massive or enterprise-wide scanning and imaging capability that allows us to input all of this into these systems later on down the road.

Then we're looking at ECI and EDI, electronic commerce. We want to be able to take the system of accounting and reporting, the integrated tax system and, in some regards, the EBT, and put them into an environment whereby we have a valid and a viable electronic commerce capability within the District. This capability can be linked to either an Intranet capability or some other application or technology that is out there that allows us to get information out to the citizens of the District, the vendors with whom we deal, the public employees and, more importantly or just as important, the key leaders who are making decisions within the District.

The last thing that we are doing is modernizing our mainframe. This is key. Without the modernization of the mainframe, we can't have a test region for Y2K testing and independent validation and verification. Nor can we have a platform or platforms that allow us to build logical partitions for the integrated tax system, for the new SOAR system, and for our comprehensive automated personnel and payroll system. We have to build additional, logical partitions so that we can accommodate this massive metamorphosis that we're going through in a very, very short period of time.

I hope that what you see from all of this is that the challenge is a huge challenge for us. It is an endeavor that we are moving out on in a new way without organization and structure we're building that as we go and without the training base we're training as we go. Through the dedication of our employees in the District, and the cooperation of our deputies who are the users and operators of these systems, I think I can tell you with a high degree of confidence that the notion of integration of information technology in a synergistic way to a business strategy is fully embraced in the District of Columbia. Thank you.

Budgeting for Local Government in the 21st Century

Dr. Abdusalam Omer, Deputy Chief Financial Officer for the Budget
The District of Columbia

What I will do in a very few minutes is wrap it up. I'll show how all these pieces fit together, particularly the revenue. We talked about the revenue. We talked about the cash issues and the deficits that we have faced. I'll give you an update as to where we are now.

Under the Control Act that was passed in 1995, the District had to submit a multi-year financial plan every year, that is to say, the current year plus another four years. So what we have is 1998 up to the year 2001, and then 1999 up to the year 2002. The premise of the Control Board to be gleaned is that the District should balance its annual budget four consecutive years. So, in that case, we have balanced the budget in 1997. We are on our way to balancing the budget in 1998, the fiscal year that just ended on September 30. Then, hopefully, with balance in another two years, the District will have total control of its destiny and its political decisions.

In this short presentation, most of you have had enough on the revenue. So we'll talk a little bit about expenditures and finally funds balance. The assets and liabilities of the District have been in the negative for a long time, and, hopefully, we will show you some of the progress we have made.

Budget expenditures for the District are $5 - 5.2 billion. Sixty-four percent of the revenues for the District come from locally generated tax, 27 percent from the Federal government, 2 percent from the intra-District, an internal type of accounting system, and 7 percent from private and other sources.

Regarding the general fund or the expenditures, along the lines of function, we see that we are spending 34 percent in wages, salaries and benefits. We are also spending 37 percent on subsidies and transfers and about 21 percent on contractual services. These are the major expenditure categories people and contractual services. Whenever we get into trouble, or whenever we need to do savings or, for that matter, improvement, it is in those two areas where we look. How do we spend the $5.2 billion? We are spending 16 or 17 percent on education, 35 percent on human services, another 17 percent on public safety, and a meager percentage on economic development. That's why the District tax base is very tight with higher taxes compared to other jurisdictions, because there is no economic development being generated. Hopefully it will be looked into very soon.

Here, on this slide, I will really give you the story of the District of Columbia. Starting in 1994 when the bottom fell out, there are a couple of lines that are very important. Look at the revised surplus, the annual surplus or deficit of the year. In 1994, there was a $335 million deficit, even though we started with a positive fund balance. Looking at 1995, things had really deteriorated further in terms of the beginning fund balance of $324 million. The Chief Financial Officer, who is currently running for the Mayor of the District, came into place, starting with the 1996 budget cycle. Since then, there has been a great improvement. We are projecting a minimum of $273 million surplus at the end of 1998, and we are also projecting that we will be able to eliminate the accumulated deficit once the books are closed and my friend Tony Pompa completes his clean audit. That's really a dramatic change for any government, particularly for a government that was so dysfunctional and so behind in technology and not collecting taxes and not controlling expenditures. To make such a turnaround is truly a dramatic story to tell.

It is also interesting to look at where we go in the out years. In 1998, we are at almost $273 million surplus. In 1999 that surplus immediately shrinks to $41 million, and as you go into the out years, it gets smaller and smaller. What it tells you is that the expenditures are growing faster than the revenues. On a cumulative basis, the expenditures are growing between 1.8 to 2 percent faster than the revenues. Here you have another struggle, I guess, as all other governments struggle. You either have to raise your revenue or reduce your expenditures. There is no in-between. So by the beginning of the year, we'll be presenting to the new Mayor, new Council and the Control Board options to consider in the financial plan for the remainder of the century and the beginning of the next century.

I would like to show you just how much improvement we've made compared to last year at this time. At the end of 1997, the cash position was a $200 million negative. Currently, it is at $230 million. In 1997, we borrowed $400 million, that's the cash we start with, running the government on a short-term basis. We will be borrowing only $200 million. That's a 50 percent reduction. That means we have more cash on hand. In the prior year, we had a 30-day average pay. This year it is a 21-day average pay. The credit ratings have also improved. There is really a true story to tell here of determination and cooperation among District officials, the Federal government and all the parties involved.

All the good news that you have seen was not only done by us. As Tom Huestis talked about, the relationship between the Federal government and the city government has changed. The state-like functions that the District had been doing were transferred back to the Federal government effective October 19, 1997. Specifically, in 1998, the Revitalization Act contributed to our recovery because there was a $201 million net savings to the District. In other words, we transferred the pension liability, courts and all the state-like functions, but, on the other hand, the District lost the traditional $660 million annual Federal contribution. The net impact of those two, the Federal government taking back the state-like functions and then eliminating the Federal government was $200 million. Specifically, the $5 billion unfunded pension liability has been relieved from the District. These are pension liabilities that have accumulated over the years. It includes all the teachers, firemen, police officers, Secret Service, park police a lot of retirees over the years. What we expect to have is increased investment in the infrastructure. In order to have a viable economic development program, the infrastructure has to be improved, i.e., transportation, school buildings, police stations, fire stations, and just taking care of day-to-day quality of life issues.

This concludes our formal presentation.

Managing Finances in the 21st Century City/State

Panelists:

Dr. Abdusalam Omer, Deputy Chief Financial Officer for the Budget
The District of Columbia
Natwar M. Gandhi, Deputy Chief Financial Officer for Tax and Revenue
The District of Columbia
Anthony Pompa, Deputy Chief Financial Officer for Financial Systems and Controller, The District of Columbia
Tom Huestis, Deputy Chief Financial Officer for Finance and Treasurer
The District of Columbia
LaMont Wells, Chief Information Officer, The District of Columbia

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MR. EINHORN (United States): As a citizen of the United States and of the District of Columbia, in the Chevy Chase section of the District of Columbia, I'm very curious. How much of this has been presented to individual Congressmen and to Congressional committees?

DR. OMER: We continually update decision makers such as the Congress on our progress. We make presentations periodically, both in writing and in person. The interim CFO goes to the Hill and explains this plan. They are well aware of the progress that the District is making.

DR. GANDHI: If I can add something here, I think the *Washington Post* has given a very favorable report on the transformation that the city has gone through on its financial front. So, I think it is rather widely known that the city has turned the corner on the financial front.

MR. DURNIL (United States): If the CFO does become Mayor, do you think that will have an accelerating impact on the success of your efforts? If he is not elected, do you think it will go backwards?

DR. GANDHI: I think the major challenge for all of us in this CFO shop is to make sure that the changes that have occurred are truly institutionalized, that they become a cultural aspect of the city's financial arena. That is a major challenge, and I think the initiatives that have happened on the personnel front and on the systems front are here to stay. And the system that Mr. Wells talked about will have a profound impact on the city's financial viability.

DR. OMER: I just want to add that the attraction of District residents to Mr. William's candidacy is that we always talk about three deficits in the District. There is a human deficit and there is infrastructure deficit and there are budget deficits. I think we solved the budget deficits and, as Dr. Gandhi said, it is a matter of institutionalizing and moving forward. We're not going back to bad financial practices. We will solve the infrastructure and the human deficit. The thing that makes Mr. William's candidacy attractive is that people are hoping he can repeat what he has done on the financial side in the service delivery side. If he is not elected, I think this train will still move forward.

MR. HUESTIS: Just to add one more thing, there is a lot of dysfunction still in many of the District agencies. You've seen a little bit about where we came from, our plan and where we are at this point. Each of the agencies has not progressed as far as some of the ones that were discussed here. There is a tremendous opportunity for improvement for the new Mayor to bring a sense of urgency and some critical thinking and a plan to clean up and reform some of the other service delivery agencies.

MR. DYE (Canada): I'd like to first congratulate you on the financial management leadership. Not being an American, I find what you've done quite impressive. However, you say your revenue streams are inhibited because you can't tax Federal properties, religious properties, universities, etc., etc. And yet, there is a very large grant in your revenue coming out of the Federal government. Is that a sort of a grant for the services the city provides such as water, policing, etc., etc.?

DR. OMER: No, that 20 percent of the revenue on the Federal side is still for state-like functions that we are doing. The 70 percent Federal contribution is for Medicaid, school lunches, Title I, etc. So the 27 percent is basically the same proportional amounts that other states get for these functions.

MR. DYE (Canada): So municipal services are a free good, are they, to all these agencies?

DR. OMER: That is correct. That is really where the disconnect is.

DR. GANDHI: And if the true costs were to be taken from the Federal government, it would amount to about $1 billion in terms of all the services that are provided to the Federal government. I think the latest case of St. Elizabeth's Hospital is a classic example of how the city truly subsidizes the Federal government.

MR. HUESTIS: Just another example, coming from a credit market background, is that each of the surrounding jurisdictions of the District is an AAA-rated entity. The State of Maryland and the State of Virginia, Arlington and Alexandria have the highest credit ratings anywhere in the country, and the District has the lowest credit rating of any major municipality in the country. So you can see by the rules of the game, all the surrounding jurisdictions have benefitted to the detriment of the District.

DR. OMER: And just another point on the micro level. The costs for John Hinckley, who is housed in St. Elizabeth's, are paid by the District government, the same as other Federal detainees.

MS. ROBINSON (United States): I'm very impressed with the financial picture that I've seen here. It is still a little difficult to get a handle on the full range of District financing of the different services that go on in the city. I was walking to the National Gallery of Art a couple of weeks ago and I saw this big sign that said, The new wing that is being added to the gallery, and I'm pretty sure it was a Federal building, is being financed with District of Columbia revenue bonds. That one sort of intrigued me, and I'm curious as to how the District can manage to finance things for the District, and then do these things for the Federal government, too. Do you get additional money for that? Why District revenue bonds?

MR. HUESTIS: That's a very good question. That's actually a function that's handled inside my office. The District provides a service to nonprofit entities that are located in the District of Columbia. As many of you know, local governments are able to finance their capital infrastructure on a tax-exempt basis, and the earnings on the interest is not taxed by the Federal government. That allows municipalities to borrow at a lower rate. The Federal tax law also allows specific not-for-profits, that are set up under the tax code 501C3, to also borrow on a tax-exempt basis. So, what has happened in this instance is that the museum has set up a separate subsidiary, a not-for-profit subsidiary, where they are allowed to take in revenues, primarily from gift shops and other activities, and are allowed to borrow against that. The District merely acts as a conduit to allow them access to tax-exempt financing. So, the District's revenue is not securing the debt. It is the museums, and the District is acting as a legal conduit to allow them to access. We're not pledging our credit. We're not doing anything but providing a service, because we do want museums and other not-for-profits to flourish and bring jobs to the District. They pay a fee to us as well.

MR. WESBERRY (United States): In looking at this, it is very similar to what I have seen in a number of countries in Latin America where I have worked for many years the need for the reform and the reform. A couple of things that are interesting are that you first had to get rid of a lot of people and you had to retrain a lot of people. You had to hire outside consultants in at least three different instances. Were they different accounting firms, or the same firms?

MR. POMPA: Three different firms.

MR. WESBERRY (United States): In other words, you were using a tremendous amount of outside consultants, which sometimes is resisted in a country which would rather do things on their own. You also had a lot of people working in parallel, keeping the old system going while you were putting up the new system. Is that right?

MR. POMPA: That's correct.

MR. WESBERRY (United States): It seems to me what you've done, if documented, would be a good manual on how to go about a comprehensive reform for a large city, state or national government. Some of you are from other countries. What do you think about that?

DR. GANDHI: Well, I would say that the guiding philosophy here was to attend and address a major financial emergency, and Mr. Williams' objective here was to accomplish a few things in a short time period. To do that, he was willing to explore whatever ways it could be done, internally, externally or a combination. Likewise, in the tax area, he decided we should do what we could internally, but if we found we couldn't do it, don't hesitate to ask for help, because the ultimate objective is to serve the taxpayers.

MR. WESBERRY (United States): Without the emergency, it probably wouldn't be possible.

DR. GANDHI: It would have been difficult to sell.

MR. HUESTIS: It was chaos. We were moving at 90 miles per hour in parallel directions, competing for resources and keeping our sense of urgency. It was kind of controlled chaos. I do think you're right. There is a model here that we've built that will allow or could provide a road map or guidance for other states and municipalities for pulling itself up. I think you're absolutely right.

MR. HAMILTON (United States): Perhaps you can contribute to the literature at an appropriate time, and perhaps summarize some of what you've done for the use of others.

We've heard so much about the dysfunctionality of the District of Columbia and what they've had to support. It sounds to me like a lot of that dysfunction has been harmonized now with taking some of these state functions out of the government. However, you still have the Secret Service, which protects the President, and you still have the Park Service functions in the District, and you're subsidizing the Federal workforce with all the services to the tune of $1 billion. So it sounds like you still have some work to do in restructuring. We wish you luck in that regard.

Another point worthy of making is that if you look at these functions; taxing, improving local government financial information, financing government, budgeting, information technology, this is the basis of the Consortium. It's good that we have this group of technocrats that come from our purview, our camp, and that they have been the ones who have turned around the District of Columbia government.

The Current Global Financial Crisis: The Challenge Ahead

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This is the time for brief commercial announcements, so here comes one. The United States Agency for International Development (USAID) is the largest financial cosponsor of this particular conference. USAID has sponsored or cosponsored both the Miami conference and the Washington conference, Miami for eight years and Washington for the last three or four years, through the Regional Financial Management Improvement Project now called Americas' Accountability/Anti-Corruption Project. It is financed by USAID and, of course, contracted to us at Casals & Associates. Our Internet address is http://www.respondanet.com. Take a look when you get back to your computers.

We are setting up an electronic newsletter. You may have noticed that our English-language newsletter which was passed out here, *Accountability/Anti-Corruption*, had a note down in the corner that said, This may be the last one you receive. We probably will not publish the English newsletter unless there is an upsurge of money. We will continue the Spanish-language newsletter which I hope you are already receiving. If you are not receiving it, in the Spanish newsletter out there, there is a postcard. If you will fill it out and give it to me, we'll get you on the mailing list.

The Spanish newsletter will continue, but in the English language we will have an electronic newsletter on our Web site, and an optional e-mail newsletter. It will not be as extensive as the one you picked up here, but we already have an AAA flash, which are little flashes of news on our Web site, and we will have a more extensive English-language newsletter with news about financial management, accountability and anti-corruption. Someday, both the English and Spanish newsletters will be electronic, but it will probably be a few years. At any rate, I wanted to share that with you, and make sure you have our Web site. My own personal e-mail is jimwes@casals.com. Both Internet addresses are in the newsletter. Do not hesitate to get in touch with us, and, of course, if you live in Latin America or the Caribbean, we work for you as long as this project continues.

Now, on the program is a closing entitled, The Current Global Financial Crisis: The Challenge Ahead. I started to get a speaker on this closing topic, but decided instead to schedule it as an open forum to fill in our remaining time.

I just want to say a few words to open the discussion and ask you what you think about the current financial crisis going on in the world today, and how it affects government financial management across the world and in your country in particular. We had 182 countries' Finance Ministers and Central Bank Governors in Washington this week. It is the Consortium's custom to have this conference follow the annual meeting of the World Bank and IMF. The dates of our 1999 conference are the Thursday, Friday and Saturday following the World Bank/IMF meeting. If you want to come on Monday, and if you can work it out with your government, you can be an observer at the World Bank/IMF meetings.

At this year's annual World Bank and IMF conference earlier this week, there was extraordinary dissension and disagreement about whether the strategy for stopping global economic turmoil has been misguided, according to press reports.

One thing that I've noticed in my years in Latin America, if a Finance Minister makes an announcement that there is definitely not going to be a devaluation, you can count on a devaluation within five days. I have seen that happen over and over again. It happened this year in Columbia, and it happened again in Ecuador in the last two months. As a matter of fact, when it happened in Ecuador, I read it on the Internet and I sent an e-mail to my brother-in-law in Quito, saying, There's going to be a devaluation. Don't change any money. Don't make any financial transactions. They will hurt you. And sure enough, the Finance Minister said it on Thursday, and in the middle of the night on Sunday night, they announced the devaluation. Well, guess what the head of the IMF said this week? He said, We are not in 1928. We are not in 1928. Well, chronologically, we're not. Most of us wouldn't be born. You know, maybe we are in 1928, but not chronological speaking. He was speaking about a worldwide depression.

The world markets are in such a turmoil that it could well be that we're going to have the worst financial crisis since 1928. What triggered it is the Long-Term Capital Equity hedge fund which nearly collapsed. Just one week before the World Bank/IMF meetings, suddenly the world knows. It comes out in *The Financial Times of London* and *The Wall Street Journal* that 18 major banks quietly met with the New York Federal Reserve. That was a startling thing in itself, that the Federal government would bail out Long-Term Capital Equity which is a hedge fund. This shocked the markets of the world and caused the panic that we've seen in the last couple of weeks. We find out that bankers all over the world raised $3-1/2 billion to bail out this fund which had a capital of $6 trillion. They didn't do this because they liked us or to save the United States or to save your country. They did it because the major banks in the world figured that if one organization collapsed, it could bring down the entire world financial system. So they got together and raised $3-1/2 billion. It is now public information and it's been in all the financial press.

Within a few days, a Swiss bank announced that they were on the verge of collapse. Another hedge fund is shaky. One of the most frightening things about it is that this long-term capital outfit, which had assets (or liabilities they thought they had assets but what they had most was liabilities) in the trillions, represents 1 percent of all hedge funds in the world. So the world is in great turmoil, and we may see an economic collapse.

We certainly are seeing a market yo-yoing, going up and down. The New York Stock Exchange has never gone up and down like it's doing now. The Tokyo exchange has also been doing that. The U.S. dollar dropped the day before yesterday. In relation to the yen, it was the greatest drop in 25 years. But the yen was low. So what we're seeing is all kinds of uncontrollable fluctuations.

How is that going to affect governmental financial management? James Wolfensohn, head of the World Bank, said that as markets tumble and as the poverty numbers soar, all of us have a shared responsibility and a shared interest in promoting prosperity and developing emerging markets. As markets tumble and poverty numbers soar, all of us have a shared responsibility to put in place policies that can help these countries work their way out of crisis. Wolfensohn said that if we do not have greater equity and social justice, there will be no political stability, and without political stability, no amount of money put together in financial packages will give us financial stability. He said that we must adjust to the crisis so that mathematics will not dominate humanity. Without building political support for the bailout programs that have led to government austerity and unemployment, according to Wolfensohn, we may build a new international financial architecture as called for by President Clinton, but it will be a house built on sand.

Every major crisis in the world has produced, as I said when we opened this conference, improvements in governmental financial management. We heard the District of Columbia say they had this terrible crisis. I'm sure you probably saw some of that in your countries over the last two or three years. That crisis enabled the D.C. group that we have here today, and two more that weren't with them, to carry out some rather interesting improvements. The Crash of 1928 resulted in the Securities and Exchange Act of 1933, improving financial management in the private sector of the United States. It has been copied throughout the world. So we may be on the verge of an opportunity even if we're on the verge of a crisis.

Does anyone else have any questions or comments?

MR. DYE (Canada): Jim, I don't think the financial managers in governments around the world will have any influence whatsoever going into the crisis. I think they'll be completely ignored. The Fund and the Bank will rely on economic advice which is not founded on accounts, much to my discouragement. The people who are making these policy decisions don't rely on financial management information. They seem to have their own sources and their own estimates. Even if a country has wonderful financial management, I don't think that's going to have an impact on a crisis. If there is a crisis, there will be a reaction. I don't think the District of Columbia would have done what they did if they really hadn't hit the wall. They responded in a very proactive way. It may well be that some good comes out of it, but going in, I think we're at the mercy of the economists and the politicians.

MR. WESBERRY: But won't people who have good financial management systems be in better shape than people who don't have good information?

MR. DYE (Canada): I think going into a worldwide financial crisis, it is more important for countries to have good banking supervision, banking regulations and national financial policies to control their expenditures. Where we come out as the financial managers is at the tail end.

MR. WESBERRY: I certainly agree with that. Let me ask Alberto Arolfo, who just stepped down as Accountant General of Argentina. I understand when former Argentine Finance Secretary Ricardo Gutierrez was in Washington recently, he surprised the bankers by telling them Argentina survived the Mexican crisis in 1996 because of their financial management system. How do you feel about the effect of the information you had, and the fact that Argentina overcame a crisis when everybody else was saying that Argentina's money was going to go down?

MR. AROLFO (Argentina): In the first days in January 1995 we already had information about our budget execution and information concerning the debt Argentina had up to the 31st of December of the previous year. This information, that we provided to Minister Cavallo and Secretary Gutierrez facing the crisis, evidently surprised the international banking world. This was thanks to the new financial administration system that we implemented in the year 1993. I feel all the countries in the world, when they can handle the financial information that comes out from the accounting records and from the budget, will have the tools they need to face crises such as the one we're seeing nowadays. Thank you very much.

MR. WESBERRY: One further comment. The eyes of the world are on Brazil. Brazil is the country in crisis at the moment, not Argentina. Several other countries are on the list to fall before Argentina. They may all fall. There are a lot of predictions that all the Latin American countries will fall like dominoes, but Argentina is way down the list because of the reliable information they have.

I know the economists and politicians don't pay attention to us. What I am saying, Ken, is when there is a collapse, they begin to realize how important reliable information is. After the collapse, there is an opportunity. So there may be a great opportunity in the very beginning of the new century to improve financial management in a lot of countries.