



# How Going BACK TO THE FUTURE<sup>1</sup> WITH OMB A-123 ←... ] CAN RESTORE TRUST IN GOVERNMENT

By Mike Wetklow, CGFM, CPA

In 1985, Hollywood released a blockbuster movie called *Back to the Future*, about the time-traveling adventures of Marty McFly and Doc Brown in a souped up DeLorean. Coincidentally, the Eighties were a time of greater trust in government than we know today, yet we do have a vehicle to get back there. With Office of Management and Budget (OMB) Circular No. A-123, we can restore public trust in government and prepare the accountability community for the future — because, in the words of Doc Brown, “Where we’re going, we don’t need roads.”



## Back in time

Going back to 1981, A-123, *Internal Control Systems*, was one of the first modern accountability policies since Watergate and the Inspector General Act of 1978. The short, five-page policy was issued in response to a Government Accountability Office (GAO) report on widespread internal control weaknesses in the federal government. It called on “all levels of management to involve themselves in assuring the adequacy of controls” and mandated ongoing evaluation of all systems. Agencies were required to establish internal control directives and plans and send reports to agency heads. Although it did not establish external reporting requirements, the circular alluded to their development along with other “specific internal control guides.” It also included a sunset provision to review the policy three years later. Fortunately, it withstood the test of time and has evolved into one of OMB’s most successful flagship policies.

OMB  
A-123

### *Internal Control Systems*,

October 28, 1981: “Agencies shall maintain effective systems of accounting and administrative control. All levels of management shall involve themselves in assuring the adequacy of controls. New programs shall be designed so as to incorporate effective systems of internal control. All systems shall be evaluated on an ongoing basis.”

The following year, Congress reinforced OMB’s efforts by passing the Federal Managers Financial Integrity Act (FMFIA), which required GAO to establish standards for internal control and OMB to establish implementation guidance. FMFIA also created what is known today as agency head assurance statements. Shortly after passage of FMFIA in December 1982, OMB published detailed internal control guidelines as a key component of the Reagan Administration’s *Reform 88* agenda.

In 1983, GAO issued the first *Standards for Internal Control in the Federal Government*, and OMB updated A-123 to align with FMFIA, including definitions for material weaknesses in internal control. In 1986, A-123 acknowledged the federal government’s evolving internal control structure by introducing management control plans that allowed OMB to move beyond financial administrative control silos to manage agency FMFIA implementation efforts. A-123 covered provisions for “alternative internal control reviews, which included computer security, financial system reviews, Inspector General audits and other management consulting reviews.”

OMB  
A-123

### *Internal Control Systems*,

August 4, 1986: “In order to streamline the process of reviewing internal control systems and to better involve program and administrative managers, Circular A-123 encourages agencies to use alternatives to the internal control review process...; e.g., computer security, financial system reviews, Inspector General audits, and other management consulting reviews.”

Fast forward to 1995, when A-123, *Management Accountability and Control*, rescinded detailed implementation instructions required within the internal control guidelines and rebranded the circular to focus on broader “management controls.” (The 1985 circular had reflected the performance emphasis of the Clinton Administration’s *National Performance Review* agenda and the passage of the Government Performance and Results Act.) While much detail was removed, the circular improved governance through a cross-functional senior management council. In addition, it provided agencies flexibility to draw conclusions on their internal control reporting through a wide variety of “sources of information,” ranging from audits of financial statements to information technology reviews to program evaluations.

OMB  
A-123

### *Management Accountability and Control*,

June 21, 1995: “Management accountability is the expectation that

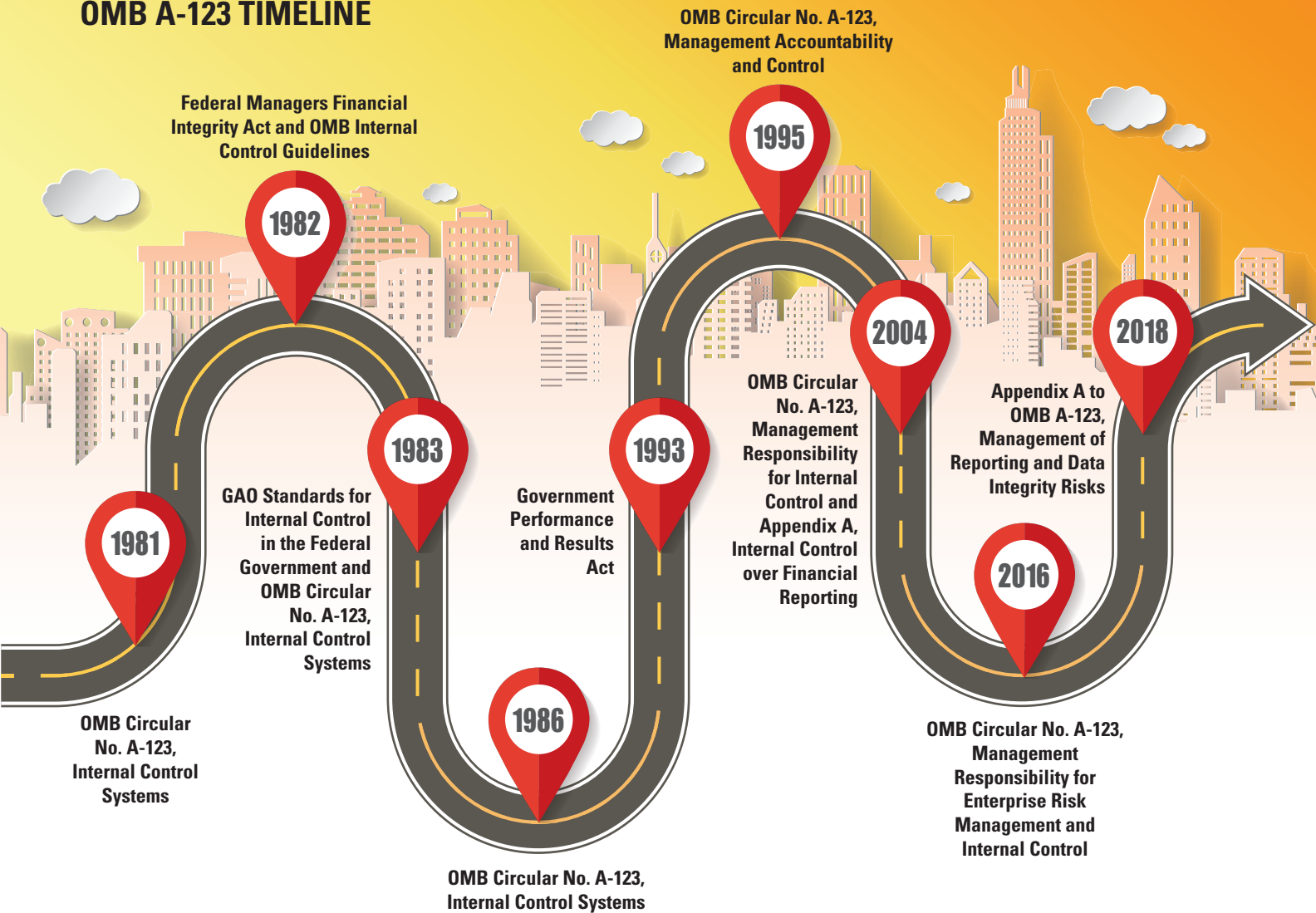
managers are responsible for the quality and timeliness of program performance, increasing productivity, controlling cost and mitigating adverse aspects of agency operations, and assuring that programs are managed with integrity and compliance with applicable law.”

In 2004, the policy pendulum swung back to detailed requirements with A-123, *Management’s Responsibility for Internal Control*. At that time, the private sector was reeling in response to Enron-type scandals and passage of the Sarbanes-Oxley anti-fraud law. The accounting profession had been self-regulated prior to Sarbanes-Oxley, which established the Public Company Accounting Oversight Board to “oversee audits” and “protect investors.”<sup>2</sup>

In the federal government, OMB doubled down on efforts to protect taxpayers with Appendix A to A-123. The supplement strengthened requirements for assessing internal control over financial reporting (ICOFR). Most interesting about this version of the circular, though, was its influence in averting cumbersome legislative requirements. Through the Department of Homeland Security Financial Accountability Act, Congress also authorized two studies — one by the Chief Financial Officers Council (CFOC), the other by GAO — to weigh the feasibility of federal ICOFR audits.<sup>3</sup>

The CFOC responded with a study that found “the value and benefit of rendering a separate opinion on ICOFR must be balanced against the added costs.” The council also developed a detailed guide recommending Congress allow OMB and agencies to determine the best way to implement ICOFR. The OMB-CFOC effort was a major government-wide success. Most agencies involved went on to earn clean financial statement audit opinions; and no additional legislation

# OMB A-123 TIMELINE



like Sarbanes-Oxley came about. However, one downside to the 2004 version of the circular was the loss of broader emphasis on performance or traditional management controls, because it became known as a financial reporting or Chief Financial Officer (CFO) effort.

Like the Sarbanes-Oxley era, the period between 2011-2015 also saw federal agencies reel from numerous high-profile internal control failures, ranging from conference scandals and veterans health care delays to tax targeting and failed health care website rollouts. All of these scandals involved internal control issues beyond financial reporting, and several agency heads resigned in their wake. OMB worked with the President's Management Council to encourage agencies to consider whether management challenges beyond financial reporting could have been avoided, minimized, or made more manageable, and what would come next.

To assist agencies with these broader risk management issues, on July 15, 2016, OMB issued the latest update to A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*. Initiated to correspond with GAO's update of the *Standards for Internal Control in the Federal Government*, it built upon past success and modernized agency FMFIA efforts. The circular drew from many lessons learned over the years, including a phased maturity-based approach to implement risk profiles and an emphasis on performance management and decision-making. It also encouraged agencies to move beyond ICOFR by requiring a separate financial assertion in the agency head assurance statement.



**Management's Responsibility for Internal Control**, December 21, 2004: "A re-examination of the existing internal control requirements for federal agencies was initiated in light of the new internal control requirements for publicly-traded companies contained in the Sarbanes-Oxley Act of 2002."



### Management's Responsibility for Enterprise Risk Management and Internal Control, July 15, 2016:

"The administration has emphasized the importance of having appropriate risk management processes and systems to identify challenges early, to bring them to the attention of agency leadership, and to develop solutions."

## Preparing for the future

In March 2018, OMB released the President's Management Agenda (PMA): *Modernizing Government for the 21st Century*, which "lays out a long-term vision for modernizing the federal government in key areas that will improve the ability of agencies to deliver mission outcomes, provide excellent customer service, and effectively steward taxpayer dollars on behalf of the American people." The PMA also notes that public trust in the federal government continues to decline toward historic lows.

## Our past can illuminate our future

A-123 experiences from the past can support the PMA and further support the community's ongoing transformation efforts to prepare for the future. The following areas are critical for government financial managers to address now.

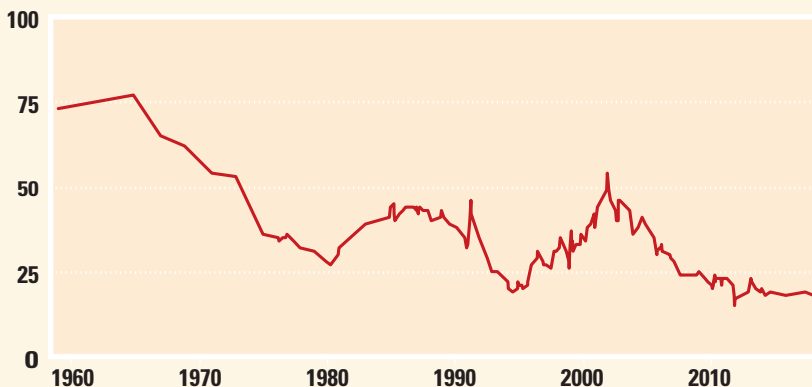
- 1. Working across silos:** The PMA states: "To really get traction on these complex and interconnected challenges, broader, system-level thinking is needed to tackle interconnected barriers." Working across silos, simply put, is "good governance; achieving intended outcomes while acting in the public interest at all times."<sup>4</sup> The 1995 version of A-123 introduced the concept of a senior management council. From an ERM perspective, it means getting the right "C-suite or CXO level executives" around the table<sup>5</sup> to assess risks and opportunities and "form a powerful guiding coalition" to ensure the new PMA does not fail.<sup>6</sup>
- 2. IT modernization — reducing cybersecurity risks to the federal mission:** The recent Cybersecurity Executive

Order<sup>7</sup> and the PMA component, *Reducing Cybersecurity Risks to the Federal Mission*, are similar to the 2004 efforts to put teeth into financial reporting through A-123. Cybersecurity is one of the top risks on agency ERM profiles; however, Chief Information Officers cannot do it alone. Today, they share with CFOs a great opportunity to work with program offices on related Federal IT Acquisition Reform Act endeavors.

- 3. Data, accountability, and transparency:** A-123 strategies from years past can support the decision-making and accountability component of the PMA. The inaugural A-123 asked agencies to develop internal control plans. This mandate was repeated in 2004 in Appendix A. As a result, financial reporting risks at agencies became largely under control. The latest Appendix A, *Management of Reporting and Data Integrity Risks*, offers a chance to take Data Act reporting to the next level by developing data quality plans that build consensus with auditors. Management, then, could move beyond low-value compliance discussions to high-value data decision-making discussions.
- 4. Shifting from low-value to high-value work:** The PMA led both OMB and agencies to propose "Congress free up tens of thousands of hours...for time better spent pursuing mission outcomes."<sup>8</sup> The solid strategies of this PMA component can be reinforced by ERM. The most important part of ERM is a "series of conversations on two key questions: 1) what are the risks facing our agency that could prevent our mission goals; and 2) how can we mitigate the impact of the most serious risk?"<sup>9</sup> As existing guidance is evaluated, burden methodologies developed, and targets set to reduce compliance burdens, ERM will be a critical factor in successfully identifying workload reduction opportunities and justifying decisions.
- 5. Results-oriented accountability for grants:** The PMA calls for "federal agencies to maximize the value of grant funding by applying a

## Public trust in government near historic lows

Percentage who say they trust the federal government to do what is right just about always/most of the time.



Notes: From 1976–2017 the trend line represents a three survey moving average.

Source: Survey of U.S. adults conducted Nov. 29–Dec. 4, 2017.

Trend sources: Pew Research Center, National Election Studies, Gallup, ABC/Washington Post, CBS/New York Times, and CNN polls.

Pew Research Center

risk-based, data driven framework that balances compliance requirements with demonstrating successful results for the American taxpayer." The 2016 version of A-123 intended to address this ongoing challenge in *Managing Grant Risks in Federal Programs*, which introduced the concept of extended enterprise (EE). Not new to other governments ahead of the U.S. on ERM implementation, EE can advance maturity in managing risks with state and local governments and, most importantly, making decisions on limited resources.

**6. Getting payments right:** Improper payments epitomize reasons citizens' trust in government has been compromised. Unfortunately, after countless legislative efforts and guidance updates, improper payments remain an elusive bugaboo. ERM can help here in two ways. First, the recent A-123 and the GAO fraud framework each introduced concepts of risk appetite and tolerance. While any conversation on risk to taxpayer resources is difficult, a discussion is needed on taxpayer resources spent on compliance outcomes that do not make sense, such as material weaknesses vs. control deficiencies vs. risk beyond federal control. Second, the first A-123 in 1981 called for "new programs to be designed so as to incorporate effective systems of internal control." In the area of improper payments, this entails conversations with Congress, the Administration, and the audit community about risks in legislation for new programs, plus serious consideration of program integrity proposals. An ERM approach could help untangle complex extended enterprise relations and also guide Congressional stakeholders in risk management as new programs are established.

**7. Consensus with auditors:** While not directly discussed in the PMA, good relations with the audit community are more important than ever to increase trust amidst the long-standing challenges government faces. An inherent apprehension of discussing risks with auditors exists among managers; however, the recent A-123 calls for change: "Agency managers, Inspector Generals, and other auditors should establish a new set of parameters encouraging the free flow of information about agency risk points and corrective measure adoption." The GAO Comptroller General reinforced this notion at the 2016 AGA Professional Development Training.

## Conclusion

Who knew time travel through A-123 history could be so much fun? The retrospective shows, in a period when the accountability community faces disruption as the new norm, A-123 is both a "timely and timeless" tool to "ultimately lead to a more resilient government."

*Because AGA recognizes the importance of ERM, we have established an ERM Hub, including resources for federal, state and local government officials to discover a complete picture of ERM's past and present and to glimpse at its future in government. Access it at [www.agacgfm.org/intergov](http://www.agacgfm.org/intergov).* ■

## Endnotes

1. *Back to the Future*™ is a registered trademark and copyright of Universal City Studios, Inc. and U-Drive Joint Venture.
2. <https://pcaobus.org/About/Pages/default.aspx>
3. GAO Report: Cost and Benefit Review of Internal Control Opinions (GAO-06-255R).
4. International Framework: Good Governance in the Public Sector, International Federation of Accountants.
5. COSO Embracing ERM, Practical Approaches for Getting Started.
6. Harvard Business Review, Leading Change, Why Transformation Efforts Fail.

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# ERM Hub

News  
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Learn more at  
[www.agacgfm.org/intergov](http://www.agacgfm.org/intergov)

7. Presidential Executive Order on Strengthening the Cybersecurity of Federal Networks and Critical Infrastructure, May 11, 2017.

8. President's Management Agenda, CAP Goal 6, *Shifting From Low-Value To High-Value Work*.

9. Thomas H. Stanton, Risk Management is Essential at a Time of Downsizing, Public Administration Review, 2013.



**Mike Wetklow, CGFM, CPA, is the National Science Foundation's (NSF) Deputy Chief Financial Officer and Division Director for Financial**

**Management. Prior to NSF, Mike has held positions at the Office of Management and Budget, U.S. Department of Homeland Security, KPMG, Government Accountability Office, and the Maryland Legislative Auditors Office. Mike received his undergraduate degree in accounting and his graduate degree in public administration both from the University of Maryland at College Park.**

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