Office of Inspector General

March 24, 2003
Audit Report No. 03-020

Travel, Relocation, and State Income Tax Withholding Policies and Procedures

TABLE OF CONTENTS

DATE: March 24, 2003

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SUBJECT: *Travel, Relocation, and State Income Tax Withholding Policies and Procedures* (Audit Report No. 03-020)

The Federal Deposit Insurance Corporation (FDIC) Office of Inspector General (OIG) has completed an audit of selected activities related to the FDIC's travel, relocation, and state income tax withholding policies and practices. This assignment was prompted by allegations made by a former FDIC employee. The overall audit objective was to determine whether the FDIC has adequately designed and implemented policies and procedures in selected travel, relocation, and state withholding tax areas where allegations were made.

We applied audit procedures only to those allegations we determined to be the most significant based on the risk that those issues could have significant tax consequences or impact on future FDIC operations. We took into consideration the results of FDIC internal and outside counsel's reviews of the matters. We reviewed current FDIC operations related to the allegations to ensure that our audit covered FDIC management-initiated improvements and the most recent status of the FDIC's policy and procedural updates. Our audit work began on October 16, 2002, and took into consideration any FDIC actions regarding these issues through January 2003. Appendix I provides details of our objective, scope, and methodology.

BACKGROUND

In April 2002, an FDIC employee submitted written allegations to FDIC management and others regarding certain activities related to the FDIC's travel, relocation, and state withholding tax policies and procedures. The Division of Finance (DOF) and the Division of Administration (DOA) administer the operational areas addressed in the allegations. DOF is generally responsible for corporate accounting and disbursements to employees and vendors; DOA is responsible for corporate personnel matters. Most of the issues we reviewed involved the FDIC's policies and procedures for alerting FDIC employees and tax authorities of all appropriate income recognition and taxable events arising from routine FDIC travel and relocation operations. Additional issues addressed FDIC employees' compliance with applicable state withholding tax laws. A summary of the criterion used to assess the issues follows:

- FDIC General Travel Regulations (GTR) – These internally written FDIC travel policies prescribe acceptable travel procedures and practices for FDIC employees who are required to travel as part of their FDIC employment.

- FDIC Relocation Regulations – These internally written FDIC relocation policies prescribe the Corporation's and relocated employees' responsibilities when official notifications of relocation are issued to initiate employee moves from one location to another.

- Title 5, United States Code – These provisions, among other things, preclude federal employees, such as FDIC Board members, from receiving any additional pay above their statutory rates.

- U.S. Treasury Regulations administered through the Internal Revenue Service (IRS) – These regulations govern employers' and employees' responsibilities for filing income tax reports and the specific rules surrounding tax-related issues.

Outside Counsel Conclusions

In addition to the FDIC internally assessing the control areas raised in the allegations, the Corporation hired the Groom Law Group (Groom) to provide legal guidance. Groom submitted its report on September 11, 2002. The FDIC's General Counsel advised the Director, DOF, on November 18, 2002, that the Groom report generally concluded that the FDIC is in compliance with applicable federal and state laws in the discussed matters. The FDIC General Counsel noted four matters where such compliance was not as clear and suggested that the FDIC consider the Groom recommendations to aid in correcting certain past errors and current ambiguities. These four areas were as follows:

(1) Spousal Travel Reimbursements,
(2) Relocation Benefits,
(3) State Income Tax Withholding, and
(4) Weekend Travel Home Reimbursements.

RESULTS OF AUDIT

The FDIC had designed and implemented policies and procedures for most of the operational areas addressed in the allegations as shown in the following table that summarizes our conclusions.

FINDING	AUDIT ISSUE	POLICIES AND PROCEDURES DESIGNED	POLICIES AND PROCEDURES IMPLEMENTED	ADDITIONAL ACTION NEEDED
A	Spousal Travel Reimbursements	**YES**	**YES**	**YES**
B	Weekend Travel Home Reimbursements	**NO**	**NO**	**YES**
C	State Income Tax Withholding	**YES**	**NO**	**YES**
D	Relocation To Specified Locations	**YES**	**YES**	**NO**
E	Chairman's Personal Goods Damage	**YES**	**YES**	**YES**
F	Relocation Benefits – Home Purchase Program	**YES**	**YES**	**NO**
G	Employee Federal Tax Compliance	**YES**	**YES**	**NO**

The following are brief descriptions of the conditions and impacts in the areas that we concluded require FDIC management's further actions.

- Spousal Travel Reimbursements. Prior to the beginning of our review, the FDIC did not have adequate controls to prevent Board Members' spouses from being reimbursed for travel expenses when those spouses accompanied their FDIC-employed partner on official FDIC assignments. While the FDIC has since designed and implemented adequate policies and procedures in this area, some past FDIC Board members received taxable reimbursements and will have to recognize additional income in calendar year 2002 and 2003 to amend the tax reporting omissions.

- Weekend Travel Home Reimbursements. The FDIC does not capture and report taxable amounts of FDIC travelers' personal weekend return trips home when it is cost beneficial for those travelers to remain on-site during extended travel assignments. Consequently, some FDIC employees received taxable travel reimbursements; however, neither the employees nor the tax authorities were properly notified.

- State Income Tax Withholding. The FDIC General Counsel concluded that the FDIC is in full compliance with laws related to withholding employees' state income taxes; however, some FDIC employees have state income tax withholding arrangements that fall outside of established FDIC policy. As a result, some FDIC employees may not be meeting their legal obligations to report state withholding taxes on income generated from FDIC employment.

- Chairman's Personal Goods Damage. A prior FDIC Chairman received a relocation-related reimbursement for damaged personal property incurred during the official relocation. Legal determinations indicate that the amount may be deemed income to the prior Chairman and require applicable reporting to the prior Chairman and tax authorities in calendar year 2003.

We are making a number of recommendations to DOF and DOA to enhance policies and better communicate the FDIC's expectations of employees with respect to corporate travel, relocation, and tax requirements; improve internal controls over travel and relocation; ensure that tax provisions are properly administered; and correct prior errors. Our audit conclusions and recommendations are consistent with the FDIC General Counsel's November 18, 2002, assessment of how to resolve the initial allegations.

FINDINGS AND RECOMMENDATIONS

Finding A: Accounting for Board Member and Spousal Travel Payments and Handling Erroneous Travel Payments

Background

The FDIC reimbursed its Board Members for their spouses' travel expenses when the spouses accompanied Board Members on official FDIC travel. It was alleged that such reimbursements were improper because the FDIC did not report the reimbursements as taxable income and the Board Members' incomes would have exceeded 5 U.S.C. § 5536 salary caps had the spousal reimbursements been properly reported.

Condition

The FDIC did not have appropriate controls in place to preclude Board Members from receiving reimbursements for their spousal travel expenses, ensure that these payments were properly reported to tax authorities, or prevent the FDIC from paying employees in excess of upper statutory salary limits. The salary overpayments violated U.S. Treasury Regulations from 1994 through 2001.

FDIC Legal Counsel, through independent contracted legal assistance (Groom) concluded that the spousal travel reimbursements are a likely violation of Title 5. However, the FDIC's treatment of the erroneous payments as debts forgiven in calendar year 2002 resolves the question as to any past violation of Title 5. By treating the Board Members' spousal travel-related amounts as debt forgiveness in 2002, none of the payments is recognized as income in the earlier years in which the travel expenses were incurred, but instead is income for 2002.

The FDIC took action to prevent similar travel transactions in the future. The FDIC revised and re-issued its Orientation Guide in January 2003. The guide now advises the Chairman and other Board Members that spousal travel will not be reimbursed by the FDIC. DOF also revised the FDIC's travel voucher audit procedures to include specific identification of any claims related to spouses and to take appropriate corrective actions. This revision was made in large part due to the October 3, 2002, OIG audit report entitled, *Controls over Board Members' Travel* (Audit Report No. 03-003). In that report, we recommended, among other things, that the DOF travel audit function specifically address the propriety of spousal travel expense claims.

In May 2002, DOF corrected the alleged prior spousal travel reimbursement errors through advisory letters that explained how the FDIC would reimburse the affected FDIC Board Members for any resulting tax obligations from the FDIC's earlier oversights. The former Board Members were informed that corrective action included treating prior taxable reimbursements as overpayments for which the FDIC has authority to waive collection. The FDIC treated the debt forgiveness as taxable income in calendar year 2002 and appropriately reported the debt forgiveness to tax authorities.

In addition to the May 2002 spousal travel corrections made by DOF, we identified $2,347 in one Board Member's spousal travel expenses while the Board Member was on travel status that also resulted in taxable amounts not appropriately reported to the employee or the tax authorities.

Criteria

U.S. Treasury Regulations require amounts paid for spousal travel to be included in taxable income. Provisions of Title 5, United States Code, define upper salary cap limits. The FDIC Legal Division determined that amounts not properly reported to taxing authorities can be treated as prior debts, the forgiveness of which establishes a taxable event in the year of the forgiveness. As further criteria, the forgiveness of Board Members' erroneous travel reimbursements is consistent with the FDIC's procedures for waiving, or forgiving, an FDIC employee's erroneous travel reimbursement during calendar year 2002.

Cause

The FDIC's travel policies allowed FDIC Board Members to claim spousal travel reimbursements under specified conditions. The FDIC's 1981 Board Resolution established the FDIC's corporate policy of reimbursing FDIC Board Members for spousal travel. FDIC Board Members were not advised that such reimbursements represent taxable income.

Effect

Improper spousal reimbursements totaling $31,825.13 occurred from 1994 through 2001. Taxable reimbursements were not reported to tax authorities in the year the expenses were incurred. The FDIC took corrective action in calendar year 2002 by treating the amounts as forgiven debt and reporting taxable amounts as calendar year 2002 income.

Conclusion

The FDIC's policies and procedures regarding Board Member spousal travel were inadequate during 1994 through 2002 and revisions are necessary. The FDIC's proposed resolution of the errors through debt forgiveness and income recognition in calendar year 2002 is appropriate. Waiving erroneous travel payments for the Board Members is consistent with the FDIC's calendar year 2002 resolution of an FDIC employee's erroneous travel payment. Thus, no preferential treatment is being afforded to FDIC executives. Regarding Title 5 violations, the issue is resolved because the FDIC treated the payments as debt, and no taxable income arose from the transaction in the year of the loan.

However, the additional $2,347 identified during our review and relating to one prior Board Member's spousal travel reimbursements during the same 1994 through 2001 timeframe has not been resolved.

Recommendation: We recommend that the Director, DOF:

(1) Treat the additional $2,347 spousal travel amount we identified as debt forgiven in 2003 and notify the prior Board Member and tax authorities accordingly, consistent with internal FDIC Legal Division conclusions.

Finding B: Managing Employee Weekend Return Travel

Background

For years, the FDIC's GTR permitted FDIC travelers to return to their duty station locations on weekends without considering whether the weekend return travel was cost beneficial to the FDIC. U.S. Treasury Regulations require that amounts must be deductible as a business expense to be excluded from employees' taxable incomes. The costs associated with return-home trips on nonworking days to visit family or for other nonbusiness reasons are generally personal and nondeductible. To comply with governing laws, employers are required to report as taxable income any amounts reimbursed in excess of the alternative costs of staying at the temporary assignment. One of the allegations was that the FDIC's policy violates those U.S. Treasury regulations, which require the FDIC to withhold applicable taxes and report as income any taxable amounts of such return trips. Specifically, the allegation was that the excess of the amount that an employee on temporary assignment spent to travel home for the weekend over the amount the employee would have spent had the employee remained at the temporary site was taxable income that was not reported to taxing authorities.

Condition

The FDIC does not capture and report taxable amounts of FDIC travelers' weekend return trips home when it is cost beneficial for those travelers to remain on-site when on extended travel assignments. The FDIC's policy of reimbursing FDIC official travelers for weekend return trips to their duty stations without requiring a determination of tax consequences conflicts with provisions of U.S. Treasury regulations.

Criteria

As explained in the Groom report, U.S. Treasury Regulations, section 1.62-2(c), regarding "accountable plans" provide that employees' travel expense reimbursements are to be excluded from an employee's income. Those regulations also include the requirement that the travel activity must have a business connection. FDIC employees' return-home trips on nonworking days are generally personal and nondeductible under the regulations, and FDIC employees are required to report as taxable income any amounts reimbursed in excess of the alternative costs of staying at the temporary assignment.

Cause

The FDIC's Travel Regulations, Section 6, allow employees on temporary assignments to return to their residence or official duty station during the course of the temporary assignment, and the FDIC had not implemented accounting controls to report the reimbursement portions subject to income taxes.

Effect

The FDIC is not in compliance with the U.S. Treasury Regulations. However, the FDIC's travel accounting records cannot accurately identify the potentially taxable reimbursements made to travelers for the prior periods during which FDIC Travel Regulations authorized expense reimbursement for employees returning to residences or official duty stations on weekends. Additionally, FDIC travel accounting records cannot generate a reasonable estimate of taxable amounts related to travelers' personal return trips. The FDIC's legal determinations, through Groom, indicate uncertainty as to whether the FDIC, as an employer, would have any liability to the IRS for failing to report income and withhold applicable taxes.

Our analyses indicate that the vast majority of weekend return trips are cost beneficial to the FDIC and would have no tax consequences to the employees. We used statistical sampling to evaluate 112 weekend return trips of 2,527 total weekend return-home trips during the first 10 months of calendar year 2002. Sampling results showed that the FDIC saved over $13,000 by having travelers return to official duty stations. Only nine weekend return trips sampled were not cost beneficial to the FDIC (return-home costs exceeded the cost of staying at the temporary assignment) and resulted in reportable taxable amounts of approximately $1,200.

Conclusion

The FDIC's weekend return-home policies and procedures do not comply with applicable U.S. Treasury regulations, and taxable amounts have not been reported to tax authorities. However, our analysis of the extent to which such trips occur and the dollar magnitude of those trips indicate that the taxes not paid are a relatively small portion of the FDIC's travel activity and expenditures. Further, our sample results are consistent with an earlier similar survey done by DOF in 1995. DOF concluded that less than 20 percent (2,432 of 12,486) of the weekend return trips were not cost beneficial to the FDIC. Our results indicate that less than 9 percent (9 of 112) of the January through October 2002 weekend returns are in the same category.

The administrative procedures necessary to correct prior errors would not be cost beneficial to the FDIC. The FDIC mission and required travel activities have remained fairly constant over the past few years, leading us to conclude that a similar travel environment existed throughout the late 1990s through 2002. In general, bank supervision and compliance matters continue to represent the largest portion of FDIC travel.

Recommendations: We recommend that the Director, DOF:

(2) Activate the capability within the Electronic Travel Voucher Processing System (ETVPS) to capture taxable amounts generated from employees' personal weekend return-home trips. ETVPS should interface with the FDIC's Central Tax Calculation and Reporting System (CTCRS) to generate the appropriate tax reporting documents at each year-end.

(3) Revise the FDIC travel policy to require travelers returning home on weekends to determine if such return trips are cost beneficial. When not cost beneficial, FDIC travelers should be required to identify those excess costs of returning home for nonbusiness purposes and report such excess amounts in the ETVPS as taxable income.

(4) Report taxable amounts related to weekend home travel to employees as taxable income after each calendar year-end in conjunction with the FDIC's preparation and issuance of employee wage and earnings statements.

Finding C: Reporting on Employee State Income Tax Withholding Status

Background

Federal agencies are required to comply with a state's income tax withholding rules with respect to employees who are subject to that state's income tax and who work in that state. It was alleged that the FDIC has allowed employees to evade state income taxes in the states in which they work and/or live by, among other things, claiming residence in states without income taxes. The allegation identified 225 such employees for calendar year 1995 who, allegedly, evaded state income tax through claiming state residency in locations other than the employees' duty stations.

Condition

The FDIC does not have adequate internal controls over monitoring FDIC employee residency records and related employee tax obligations.

Criteria

5 U.S.C. § 5517 provides that agreements between the Secretary of the Treasury and the states will require federal agencies to comply with the withholding provisions of each state's statutes or regulations. Generally, absent a reciprocal agreement, federal employers will withhold taxes for the state in which the employee works or, for all intents and purposes, an FDIC employee's assigned duty station. The FDIC summarized state income tax reciprocity agreements in Circular 2220.2, which outlines the FDIC's and its employees' responsibilities for state income tax withholdings per applicable laws.

Cause

The FDIC does not routinely monitor differences between employees' residency records provided to the FDIC's Personnel Services Branch and employees' assigned duty stations. FDIC Circular 2220.2 identifies, on a nationwide basis, reciprocity agreements between states regarding employees' state income tax obligations. Absent the FDIC's ongoing matching of employees' residences with duty stations, the Corporation is not fully complying with its own state withholding tax policies. Further, without ongoing monitoring, the FDIC has no consistent bases upon which to initiate the Circular 2220.2 prescribed actions of referring violations to the Office of Inspector General, initiating criminal prosecutions, or taking actions regarding personnel and ethical issues relative to employment with the FDIC.

Effect

As of year-end 2002, seven FDIC employees' records indicate that their residences differ from their duty stations. As a result, the FDIC did not withhold state income taxes for those seven employees in accordance with established policy in FDIC Circular 2220.2. All of the seven employees have Washington, D.C. as their official duty station. None of the seven has state income tax withholdings in Washington, D.C. or those states with established reciprocity agreements with Washington, D.C.

Conclusion

The FDIC's current policies and procedures essentially conform with the laws applying to withholding state income taxes from appropriate jurisdictions. For calendar year 2002, the FDIC identified employees with claimed legal residences that differ from their duty stations, which varied from the FDIC policy established in Circular 2220.2. The FDIC notified those employees of the address differences and obtained explanations to achieve reasonable resolutions of policy variances.

Recommendations: We recommend that the Director, DOA:

(5) Continue to perform ongoing monitoring of employees' residency records and state withholding instructions to ensure that the policy of FDIC Circular 2220.2 is in effect by comparing employees' residency addresses with assigned duty stations.

(6) Advise FDIC employees of the applicable state withholding tax laws in cases where variances are detected, provide assistance in employees' providing the appropriate residency information for tax withholding purposes, and obtain and document employee explanations and resolution of each variance.

Finding D: Ensuring that Employees to Whom Relocation Benefits Are Paid Actually Relocate to the Location Specified in Their Relocation Orders

Background

The FDIC's relocation regulations specify the maximum distance between an employee's duty station and his/her residence if the FDIC is reimbursing the relocation expenses. The allegation was that the FDIC reimbursed employees to relocate in instances where employees did not obtain residences within the prescribed distance from their newly assigned duty stations. The allegation further explained that FDIC employees would not be entitled to relocation reimbursements if the actual geographical move did not result in the employee residing within the boundaries set forth in the relocation regulations.

Condition

The FDIC did not have adequate internal controls prior to calendar year 2002 to ensure that relocation reimbursements were made only to employees who relocated to geographical locations within the boundaries indicated in the FDIC's relocation orders. In one instance, the FDIC recovered a portion of the relocation reimbursement after-the-fact because the employee violated relocation regulations.

Criteria

FDIC GTR require relocated employees to live within a prescribed commuting distance from the employees' assigned duty stations.

Cause

The FDIC has not monitored relocated FDIC employees' prior and new residence locations to ensure compliance with FDIC relocation regulations.

FDIC Response

Excluding instances of deliberate fraud, at least one prior relocation error involved improper reimbursements to an employee whose relocation was not done in accordance with FDIC relocation regulations. The FDIC took action to recover a portion of the relocation reimbursement. Recent FDIC relocations, however, indicated that FDIC employees complied with the relocation regulations. For January 1 through August 31, 2002, all FDIC relocated employees obtained new residences within the prescribed commuting distance defined in the FDIC's relocation regulations.

Conclusion

The FDIC has initiated proper control activities to prevent FDIC employees from being reimbursed if their moves violate FDIC relocation regulations. The full compliance noted for all January 1 through August 31, 2002, relocations and assurances from FDIC management that ongoing monitoring is now in place support our conclusion. The single prior instance of policy noncompliance was resolved appropriately by FDIC management. We have no recommendations related to this issue.

Finding E: Tax Reporting Concerns Raised to FDIC Management – Prior FDIC Chairman's Reimbursement for Personal Damages During Relocation

Background

The FDIC authorized a $2,610 reimbursement to a former Chairman for personal goods damaged during the Chairman's official move to Washington, D.C. It was alleged that the amount was taxable and not reported. Also, it was alleged that the FDIC has never paid any other household goods damage claim, because household goods are the responsibility of the relocating employee and the carrier.

Condition

The FDIC's reimbursement of damages incurred during a prior FDIC Chairman's relocation were not reflected in taxable income and may have provided the prior Chairman with a form of compensation that, combined with salary, exceeded the Title 5 federal executive salary cap.

Criteria

5 U.S.C. § 5536 prohibits an employee whose pay is fixed by statute or regulation from receiving additional pay for any service or duty, unless specifically authorized by law. The FDIC Legal Division determined that the calendar year 1999 reimbursement made to the prior FDIC Chairman should be treated as an advance or erroneous payment.

Cause

The FDIC reimbursed damages related to the prior Chairman's relocation without fully researching and applying Title 5 provisions and the governing tax laws.

FDIC Response

The prior Chairman received a calendar year 1999 relocation-related reimbursement of $2,610 which legal guidance suggests should be reported as taxable income. As of February 2003, the FDIC was considering options for resolving the matter. Groom concluded that the FDIC could address the possible Title 5 concerns by treating the payment as a loan, forgiving the debt, and recognizing a taxable event in the year of forgiveness. Groom recommended that the FDIC take that action in calendar year 2002. The issue has now moved into calendar year 2003 without being resolved.

Conclusion

The $2,610 payment made to the prior FDIC Chairman was described by Groom as a potential violation of Title 5. The matter remained unresolved as of January 2003. The FDIC has options for resolving the matter. Resolution consistent with the FDIC General Counsel's advice would be appropriate.

Recommendation: We recommend that the Director, DOF:

(7) Take action to implement resolution of the $2,610 payment to the prior FDIC Chairman in accordance with FDIC General Counsel's opinion on acceptable resolution options.

Finding F: Tax Reporting Concerns Raised to FDIC Management – Underreported Taxable Amounts Through the FDIC's Home Purchase Program

Background

The FDIC has a Home Purchase Program to assist employees with selling their qualifying property at prior official duty stations so they can more quickly purchase a home at new official duty stations. The FDIC travel regulations provide that all relocation reimbursements are treated as taxable, and the FDIC grosses up (i.e., adjusts employees' payments upward to cover applicable taxes) the income of employees to compensate for the tax liability. The allegation indicated that, prior to calendar year 1999, the FDIC Home Purchase Program was structured such that taxable relocation reimbursements through that program were not reported as taxable income to either the employee or tax authorities. A potential $1.4 million tax deficiency was noted in the allegation.

Condition

Prior to 1999, the FDIC's accounting procedures did not ensure that FDIC employees' taxable reimbursements received under the FDIC Home Purchase Program were reported to employees and tax authorities. A total of 280 FDIC employees received a total of approximately $3.2 million in taxable reimbursed sales commissions. Taxing authorities were not notified of these payments.

Criteria

IRS Technical Advice Memorandum 8522022 requires that realty commissions and any closing costs directly paid by the FDIC on behalf of relocating FDIC employees should be included in the employees' income. Section 6501(a) of the Internal Revenue Code provides for a general 3-year statute of limitations for incorrect reporting on W-2, 940, and 941 forms.[1] Section 6501(e) extends the period to 6 years if the taxpayer omits from gross income an amount in excess of 25 percent of the amount of gross income stated in the return.

Cause

The FDIC was unaware of the taxable treatment of sales commissions paid directly to contracted brokers handling employees' home sales arrangements on behalf of the FDIC through the Home Purchase Program.

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[1] IRS Forms W-2, 940, and 941 relate to required reporting on employee earnings. Form W-2 is the annual report of wages and earnings; Form 940 is the employer's annual federal unemployment tax return; and Form 941 is the employer's quarterly federal tax return for reporting wages, and employer and employee federal tax obligations.

FDIC Response

The FDIC did not notify the relocated employees and tax authorities of the taxable commission reimbursements paid pursuant to the Home Purchase Program. The FDIC's General Counsel considered these past reporting errors and opined that there is no need to address the errors because they occurred in closed tax years. The FDIC General Counsel also concurred with Groom that DOF should remain vigilant to ensure future compliance with the applicable tax reporting requirements.

Conclusion

Our review indicated that the tax reporting inadequacies were corrected for calendar years 1999 and thereafter. We consider the issue properly resolved and are making no recommendation.

Finding G: Tax Reporting Concerns Raised to FDIC Management – FDIC Employees' Noncompliance with Federal Income Tax Provisions

Background

The IRS alerted the FDIC that 2.98 percent of FDIC employees had some type of federal income tax delinquency in the form of a balance owed and/or unfiled tax return as of October 2001. It was alleged that as many as 10 percent of FDIC employees may be in delinquency status if the separately alleged FDIC employees' taxable travel expenses going unreported (as discussed in Finding B) are taken into consideration.

Condition

As of October 2001, 2.98 percent of FDIC employees had some type of federal income tax delinquency as reported to FDIC Chairman Powell by then-IRS Commissioner Charles O. Rossotti.

Criteria

IRS's system of taxation relies on voluntary compliance. The FDIC has no statutory mandate to require its employees to comply with federal tax laws.

Cause

FDIC employees either owed outstanding federal tax obligations or had not yet filed tax returns for which filing deadlines had passed.

FDIC Response

The IRS believes that tax delinquency among federal employees can damage the credibility of the tax administration system. The FDIC agrees and issued a global announcement to all FDIC employees through the "Mercury" global messages on April 11, 2002. In that message, DOF echoed IRS Commissioner Rossotti's concerns.

Conclusion

The FDIC has taken appropriate action to notify its employees of the IRS's concern, and we are not making a recommendation.

CORPORATION COMMENTS AND OIG EVALUATION

On March 17, 2003, the DOA and DOF Directors provided a joint written response to the draft report. The response is presented in Appendix II of this report. In their written response, both DOA and DOF concurred with our recommendations. All seven recommendations are considered resolved but will remain undispositioned and open until we have determined that agreed-to corrective actions have been completed and are effective.

DOA's and DOF's responses to our recommendations are summarized below, along with our evaluation of those responses.

Recommendation 1: We recommend that the Director, DOF, treat the additional $2,347 spousal travel amount we identified as debt forgiven in 2003 and notify the prior Board Member and tax authorities accordingly, consistent with internal FDIC Legal Division conclusions.

DOF concurs with this recommendation and has taken or will complete the following corrective actions:

- On March 14, 2003, DOF initiated the same corrective measures completed last May for similar reimbursements. As part of the FDIC's tax reporting process, both the forgiveness of debt and the reimbursement representing the estimated tax cost will be reported to the IRS through a 1099-C and 1099-MISC, respectively, in early 2004 for the tax year 2003. The issuance of the 1099s will be completed as part of the normal reporting process. DOF expects this matter to be resolved no later than March 31, 2003.

Since final corrective action cannot be completed until necessary 2003 IRS tax forms are available and filed by the FDIC, this recommendation is resolved, but it will remain undispositioned and open until we have determined that agreed-to corrective action has been taken and is effective.

Recommendation 2: We recommend that the Director, DOF, activate the capability within the Electronic Travel Voucher Processing System (ETVPS) to capture taxable amounts generated from employees' personal weekend return-home trips. ETVPS should interface with the FDIC's Central Tax Calculation and Reporting System (CTCRS) to generate the appropriate tax reporting documents at each year-end.

DOF concurs with our recommendation. On March 13, 2003, DOF activated the capability within ETVPS to capture taxable amounts generated from employees' personal weekend return-home trips by establishing the "Taxable Weekend Return Travel" account under the Taxable Expense column in ETVPS. This new account provides an interface with the CTCRS system that will allow for the appropriate income tax processing and reporting.

This recommendation is resolved but will remain undispositioned and open until we have determined that agreed-to corrective action has been completed and is effective.

Recommendation 3: We recommend that the Director, DOF, revise the FDIC travel policy to require travelers returning home on weekends to determine if such return trips are cost beneficial. When not cost beneficial, FDIC travelers should be required to identify those excess costs of returning home for nonbusiness purposes and report such excess amounts in the ETVPS as taxable income.

DOF concurs with our recommendation. The revised changes to the FDIC General Travel Regulations have been drafted and approved by FDIC management, effective March 12, 2003. The policy revisions include descriptions and examples of the portions of weekend return trips that are taxable. Further, DOF prepared a Question and Answer document to guide FDIC employees in applying the new policies. The proposed policy changes have been forwarded to the Labor and Employee Relations Section, DOA, for submission to the National Treasury Employees Union (NTEU) for final clearance. Once cleared by the NTEU, a global email, the revised policy, and frequently asked questions with an example will be published. DOF expects that all actions necessary to address this recommendation will be completed by April 15, 2003.

This recommendation is resolved but will remain undispositioned and open until we have determined that agreed-to corrective action has been completed and is effective.

Recommendation 4: We recommend that the Director, DOF, report taxable amounts related to weekend home travel to employees as taxable income after each calendar year-end in conjunction with the FDIC's preparation and issuance of employee wage and earnings statements.

DOF concurs with our recommendation. The same corrective actions undertaken to address recommendation 2 are intended to address this recommendation. Specifically, as noted above, on March 13, 2003, DOF activated the capability within ETVPS to capture taxable amounts generated from employees' personal weekend return-home trips by establishing the "Taxable Weekend Return Travel" account under the Taxable Expense column in ETVPS. This new account provides an interface with the CTCRS that will allow for the appropriate income tax processing and reporting. CTCRS interfaces with ETVPS and captures amounts designated as taxable for reporting to tax authorities. FDIC employees receive notification of taxable income through the annual issuance of Internal Revenue Service forms W-2 and 1099 each January for the preceding year.

This recommendation is resolved but will remain undispositioned and open until we have determined that agreed-to corrective action has been completed and is effective.

Recommendation 5: We recommend that the Director, DOA, continue to perform ongoing

monitoring of employees' residency records and state withholding instructions to ensure that the policy of FDIC Circular 2220.2 is in effect by comparing employees' residency addresses with assigned duty stations.

DOA concurs with our recommendation. The following corrective actions were undertaken by DOA to address the monitoring of employee residences and state withholding instructions:

- To monitor compliance with applicable state tax withholding instructions, DOA's Human Resources Branch (HRB) performed a review in August 2002 to evaluate FDIC employees' residency records and state withholding instructions. HRB will continue to review and monitor employee residence addresses with assigned duty stations in an attempt to identify apparent discrepancies.

- In those instances where an error or inconsistency is identified, HRB staff will work with the employee to initiate corrective action or obtain and document an explanation for the variance. HRB expects to perform this review on a quarterly basis, and the review will be completed within 45 days after the end of a quarter. HRB will conduct a review for the first quarter ending March 31, 2003.

This recommendation is resolved but will remain undispositioned and open until we have determined that agreed-to corrective action has been completed and is effective.

Recommendation 6: We recommend that the Director, DOA, advise FDIC employees of the applicable state withholding tax laws in cases where variances are detected, provide assistance in employees' providing the appropriate residency information for tax withholding purposes, and obtain and document employee explanations and resolution of each variance.

DOA concurs with our recommendation and indicates in its response that the corrective action referred to in recommendation 5 above resolves the FDIC's method for dealing with variances in residences and state withholding instructions and advising employees. Specifically, as reflected in DOA's response to recommendation 5:

- In those instances where an error or inconsistency is identified, HRB staff will work with the employee to initiate corrective action or obtain and document an explanation for the variance. HRB expects to perform this review on a quarterly basis, and the review will be completed within 45 days after the end of a quarter. HRB will conduct a review for the first quarter ending March 31, 2003.

This recommendation is resolved but will remain undispositioned and open until we have determined that agreed-to corrective action has been completed and is effective.

Recommendation 7: We recommend that the Director, DOF, take action to implement resolution of the $2,610 payment to the prior FDIC Chairman in accordance with FDIC General Counsel's opinion on acceptable resolution options.

DOF concurs with this recommendation and took the following step to address the issue:

- On March 14, 2003, per the FDIC Counsel's direction, a letter of explanation was mailed to the prior FDIC Chairman requesting repayment of the funds paid to her in 1999 for damages caused during her household goods move. DOF expects this matter to be resolved with receipt of the funds no later than March 31, 2003.

This recommendation is resolved but will remain undispositioned and open until we have determined that agreed-to corrective action has been completed and is effective.

APPENDIX I

OBJECTIVE, SCOPE, AND METHODOLOGY

Our audit objective was to determine whether the FDIC has adequately designed and implemented policies and procedures in selected areas where allegations were made. As is more fully summarized in our Background section, we reviewed the applicable laws and regulations pertaining to each audit area. Where appropriate, we noted legal and regulatory impacts in each finding and corresponding recommendations. We also reviewed the existing internal control activities for each FDIC operational area involved in the allegations. By the nature of this audit effort to address specific allegations, the Government Performance Review Act (GPRA) performance measurements were not applicable to our audit procedures.

Each audit area is listed below along with a summary of our audit scope and methodology:

- Accounting for Board Member and Spousal Travel Payments. We verified that the spousal reimbursement amounts from the allegation that were paid to FDIC board members from 1994 through 2002 were supported by FDIC documentation. We verified that ETVPS computer-generated data could be reconciled with the FDIC's general ledger, and obtained direct access to the ETVPS computer database to determine that Board Member travel vouchers were fully accounted for from 1994 through 2002.

- Handling Erroneous Travel Payments. We reviewed the FDIC Board Members' erroneous travel payments in the allegations and evaluated the legal options available to the FDIC to resolve those errors. We obtained legal guidance from OIG Counsel and made determinations of the legal propriety of the FDIC's handling of the alleged erroneous payments.

- Managing Employee Weekend Return Travel. We reviewed FDIC policy and procedures for compliance with existing laws and regulations. To determine the magnitude of FDIC travelers' personal weekend return-home trips while on extended assignments, we made a representative selection of such weekend return trips. We queried the FDIC's ETVPS to identify the universe of weekend return trips by specifying the days of the week travel was initiated and completed. Our representative sample attribute was defined as all trips for which an FDIC traveler went home on Friday and then returned to the same assignment on the following Monday. Travelers' roundtrip return-home transportation costs were used to determine the total cost of the weekend return trip. The alternative comparative cost of staying on site over the weekend allowed for 3 nights of lodging (Friday, Saturday, Sunday), 2 full days of per diem (an approximation of Friday midnight until Monday morning), and added transportation costs. We also verified that the ETVPS data could be reconciled to the FDIC's general ledger and was therefore the complete and accurate database of the FDIC travel activity for the periods reviewed.

  Our sample of 112 items was drawn from a universe of 2,527 weekend return trips. The sample parameters were 95-percent confidence level and a plus or minus 4-percent precision level. We used ACL Services, Ltd. software to select the sample and analyze testing results.

- Reporting on Employee State Income Tax Withholding Status. The FDIC's Personnel Services Branch (PSB) performed matches during the second half of calendar year 2002 of all employees' residences and duty station locations. PSB researched differences for compliance with FDIC state withholding tax policy. Through computer-generated queries, we performed the same match independently for the Washington, D.C. duty station employees as of December 2002 and reviewed the progress that PSB had made in resolving questionable items. We also compiled a December 2002 list of residency/duty station mismatches and reviewed the actions taken by PSB to achieve resolution of the employees appearing on the December 2002 list. Our computer-generated queries were used to verify that PSB's computer matching procedures of FDIC employee address and duty station data were accurate.

- Ensuring that Employees to Whom Relocation Benefits Are Paid Actually Relocate to the Location Specified in Their Relocation Orders. We obtained a schedule of all FDIC relocations during January 1 through October 31, 2002 and compared the residential locations to the relocation orders. We consulted with PSB to determine whether those employees' newly acquired residences comply with FDIC relocation regulations regarding requirements to live within a prescribed distance of newly assigned duty stations.

- Addressing Tax Reporting Concerns Raised to FDIC Management. Three tax matters were reviewed in this audit area: (1) A $2,610 damaged-property reimbursement to a prior Chairman and the related tax consequences, (2) the FDIC's potential improper reporting of taxable amounts related to its Home Purchase Program, and (3) the FDIC's response to the IRS's request that the FDIC assist the IRS in ensuring FDIC employee federal tax filing compliance.

  For the first issue, we reviewed the nature of the transaction and the acceptable range of resolution alternatives provided by the FDIC's General Counsel.

  We reviewed DOF's analysis of the alleged payments made through the Home Purchase Program that were not reported as taxable in calendar years 1997 and 1998. We obtained Groom's, FDIC General Counsel's, and OIG Counsel's legal advice on alternative resolutions. We determined that the matter was appropriately resolved because all involved Counsel agreed on the FDIC's action to resolve the matter.

  For the IRS compliance matter, we reviewed the actions that the FDIC had taken and determined whether any additional actions were necessary.

We performed our audit from October 2002 through January 2003 in accordance with generally accepted government auditing standards.

APPENDIX II

CORPORATION COMMENTS

FDIC
Federal Deposit Insurance Corporation

March 17, 2003

MEMORANDUM TO: Stephen M. Beard
Deputy Assistant Inspector General for Audits

FROM: Fred S. Selby, Director
Division of Finance

Arleas Upton Kea, Director
Division of Administration

Arleas Upton Kea

SUBJECT: Management Response to OIG Draft Report Entitled *Travel, Relocation and State Income Tax Withholding Policies and Procedures (Assignment No. 2002-503)*

We have completed our review of the subject Office of the Inspector General (OIG) report. We appreciate the review performed by OIG and its recommendations to enhance and improve the overall travel, relocation, and state income tax withholdings policies and procedures.

The report contained a total of seven recommendations made by the OIG. Two of the recommendations were directed to the Division of Administration (DOA), while the five remaining recommendations were directed to the Division of Finance (DOF). As a result, this memorandum summarizes responses from both divisions and outlines our planned corrective actions with the expected completion dates for the management actions proposed.

We concur with all recommendations presented and offer the following specific responses.

Finding A: Accounting for Board Member Travel and Handling Erroneous Travel Payments

Finding A recommends that the Director, DOF:

1) Treat the additional $2,347.27 spousal travel amounts identified as debt forgiven in 2003 and notify the former Board Member and tax authorities accordingly, consistent with internal FDIC Legal Division's conclusions.

   DOF concurs with this recommendation. The following action has been taken to address this issue:

   - On March 14, 2003 DOF initiated the same corrective measures completed last May for similar reimbursements. As part of FDIC's tax reporting process, both the forgiveness of debt and the reimbursement representing the estimated tax cost will be reported to the IRS through a 1099-C and 1099-MISC respectively in early 2004 for the tax year 2003. The issuance of the 1099's will be completed as part of the normal reporting process. We expect this to be resolved no later than March 31, 2003.

Finding B: Managing Employee Weekend Return Travel

Finding B recommends that the Director, DOF:

2) Activate the capability within the Electronic Travel Voucher Processing System (ETVPS) to capture taxable amounts generated from employees' personal weekend return-home trips. ETVPS should interface with the FDIC's Central Tax Calculation and Reporting System (CTCRS) to generate the appropriate tax reporting documents at each year-end.

3) Revise the FDIC travel policy to require travelers returning home on weekends to determine if such return trips are cost beneficial. When not cost beneficial, FDIC travelers should be required to identify those excess costs of returning home for nonbusiness purposes and report such excess amounts in the ETVPS as taxable income.

4) Report taxable amounts related to weekend home travel to employees as taxable income after each calendar year-end in conjunction with the FDIC's preparation and issuance of employee wage and earnings statements.

DOF concurs with these recommendations. The following steps have been taken to address these issues:

- To address recommendations 2 and 4, on March 13, 2003 DOF activated the capability within ETVPS to capture taxable amounts generated from employees' personal weekend return-home trips by establishing the "Taxable Weekend Return Travel" account under the Taxable Expense column in ETVPS. This new account provides an interface with the CTCRS system that will allow for the appropriate income tax processing and reporting. We believe this action completes these two recommendations.

- The revised changes to the FDIC General Travel Regulations have been drafted and approved by FDIC management, effective March 12, 2003. The proposed policy changes have been forwarded to the Labor and Employee Relations Section (LERS), DOA for submission to the NTEU for final clearance. Once cleared by the NTEU, a global, the revised policy, and frequently asked questions with an example will be published. We expect all actions necessary to address this recommendation to be completed by April 15, 2003.

Finding C: Reporting on Employee State Income Tax Withholding Status

Finding C recommends that the Director, DOA:

5) Continue to perform ongoing monitoring of employees' residency records and state withholding instructions to ensure that the policy of FDIC Circular 2200.2 is in effect by comparing employees' residency addresses with assigned duty stations.

6) Advise FDIC employees of the applicable state withholding tax laws in cases where variances are detected, provide assistance in employees' providing the appropriate residency information for tax withholding purposes; and obtain and document employee explanations and resolution of each variance.

DOA concurs with the OIG recommendations. The following steps have been taken to correct these issues:

- To monitor compliance with applicable state tax withholding instructions, the DOA, Human Resources Branch (HRB) performed a review in August 2002 to evaluate FDIC employees' residency records with state withholding instructions. HRB will continue this practice to review and monitor employee residence addresses with assigned duty stations in an attempt to identify apparent discrepancies.

- In those instances where an error or inconsistency is identified, HRB staff will work with the employee to initiate corrective action or obtain and document an explanation for the variance. HRB expects to perform this review on a quarterly basis, and the review will be completed within 45 days after the end of a quarter. HRB will conduct a review for the first quarter ending March 31, 2003.

Finding D: Ensuring that employees to whom Relocation Benefits are paid actually relocate to the location specified in their Relocation Orders

Finding D requires no corrective action at this time.

Finding E: Tax Reporting concerns raised to FDIC management – Prior FDIC Chairman's reimbursement for Personal Damages during relocation

Finding E recommends that the Director, DOF:

7) Take action to implement resolution of the $2,610 payment to the prior FDIC Chairman in accordance with FDIC General Counsel's opinion on acceptable resolution options.

DOF concurs with this recommendation. The following step has been taken to address this issue:

- On March 14, 2003, per the FDIC Counsel's direction, a letter of explanation was mailed to the prior FDIC Chairman requesting repayment of the funds paid to her in 1999 for damages caused during her household goods move. We expect this to be resolved with receipt of the funds no later than March 31, 2003.

Finding F: Tax Reporting concerns raised to FDIC management – Underreported Taxable Amounts through FDIC's Home Purchase Program

Finding F requires no corrective action at this time.

Finding G: Tax Reporting concerns raised to FDIC management – FDIC Employees' Noncompliance with Federal Income Tax Provisions

Finding G requires no corrective action at this time.

If you have any questions regarding the above responses, please contact: Andrew Nickle, Audit Liaison for the Division of Administration at (202) 942-3190 or Stan Pawlowski, Chief, Management Services Section for the Division of Finance at (202) 416-7343.

cc: Steven O. App
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MANAGEMENT RESPONSES TO RECOMMENDATIONS

This table presents the management responses that have been made on recommendations in our report and the status of recommendations as of the date of report issuance. The information in this table is based on management's written response to our report and subsequent communication with management representatives.

Rec.	Corrective Action: Taken or Planned/Status	Expected Completion Date	Monetary Benefits	Resolved[2] : Yes or No	Dispositioned[3] : Yes or No	Open or Closed[4]
1	DOF concurs with the recommendation and initiated corrective action on March 14, 2003. The necessary tax reporting documents will be issued along with FDIC's routine reporting of FDIC employee taxable incomes at year-end 2003.	January 31, 2004	N/A	Yes	No	Open
2	DOF concurs with the recommendation and activated the capability within ETVPS to capture taxable amounts generated from employees' personal weekend return-home trips. The ETVPS will interface with the FDIC's tax reporting system to allow for income tax processing and reporting.	March 13, 2003	N/A	Yes	No	Open

[2] Resolved – (1) Management concurs with the recommendation and the planned corrective action is consistent with the recommendation.
(2) Management does not concur with the recommendation but planned alternative action is acceptable to the OIG.
(3) Management agrees to the OIG monetary benefits or a different amount, or no ($0) amount. Monetary benefits are considered resolved as long as management provides an amount.

[3] Dispositioned – The agreed-upon corrective action must be implemented, determined to be effective, and the actual amounts of monetary benefits achieved through implementation identified. The OIG is responsible for determining whether the documentation provided by management is adequate to disposition the recommendation.

[4] Once the OIG dispositions the recommendation, it can then be closed.

3	DOF concurs with the recommendation and revised FDIC travel policy, effective March 12, 2003. The proposed policy is to be published via global email communication, along with frequently asked questions and examples. The FDIC expects to complete corrective actions by April 15, 2003.	April 15, 2003	N/A	Yes	No	Open
4	DOF concurs with the recommendation and activated the capability within ETVPS to capture taxable amounts generated from employees' personal weekend return-home trips. The ETVPS will interface with the FDIC's CTCRS to ensure appropriate income tax processing and reporting each January for the preceding year.	January 31, 2004	N/A	Yes	No	Open
5	DOA concurs with our recommendation and indicated that the matching between state withholding tax instructions and employees' addresses will be done quarterly, the first match being for the quarter ended March 31, 2003. The results of the match will be available 45 days after the end of each quarter.	May 15, 2003	N/A	Yes	No	Open
6	DOA concurs with our recommendation and will review employees' residences and withholding instructions on a quarterly basis. DOA will take corrective action to resolve variances. The results of each quarterly review are to be completed within 45 days of the end of each quarter.	May 15, 2003	N/A	Yes	No	Open
7	DOF concurs with our recommendation. The FDIC made arrangements to have the prior Chairman reimburse the FDIC for the $2,610.	March 31, 2003	N/A	Yes	No	Open