

**UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL**

***STATEMENT OF THE HONORABLE PHYLLIS K. FONG
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Before the
SENATE COMMITTEE ON AGRICULTURE, NUTRITION, AND FORESTRY

March 9, 2006



Good morning, Chairman Chambliss, Ranking Member Harkin, and Members of the Committee. Thank you for inviting me to testify before you today to discuss the results of our recent audit regarding the Grain Inspection, Packers and Stockyards Administration's (GIPSA) Management and Oversight of the Packers and Stockyards Programs.

GIPSA works to ensure a productive and competitive global marketplace for USDA products. The agency's Packers and Stockyards Programs (P&SP) are responsible for maintaining fair trade practices in the marketing of livestock, providing financial protection for participants in livestock transactions, and ensuring open competitive marketing conditions for livestock and meat. Competition investigations are complex and often require sophisticated economic modeling and analyses. P&SP is responsible for evaluating complaints regarding restriction of competition, failure to compete, apportionment of territory, price manipulation, price discrimination, and predatory pricing.

In April 2005, OIG received a letter from the Ranking Member of this Committee, Senator Tom Harkin, expressing concerns with GIPSA's management and oversight of the P&SP. Of particular concern was the possible overstatement of the number of investigations that were conducted by the agency's competition division as reported in GIPSA annual reports. The number of actual investigations is an indicator of the level of GIPSA's enforcement activity for a particular year. In response to this inquiry, we

initiated an audit to evaluate GIPSA's management and oversight of P&SP.¹ Specifically, our audit evaluated the adequacy of GIPSA's actions to (1) investigate and act against anti-competitive activities, (2) count and track complaints; (3) strengthen program operations; and (4) allocate and use resources for conducting investigations.

To accomplish these objectives, we conducted our audit work at GIPSA Headquarters in Washington, D.C., and each of the agency's three P&SP regional offices from May to October 2005. We evaluated current investigative policies and procedures and examined pertinent documentation. The documentation we examined included records from P&SP's investigative tracking system, investigative work plans and reports, weekly activity reports, and records of employee turnover and retention. We also interviewed over 50 current and former GIPSA employees and the Assistant General Counsel for Trade Practices with the Office of General Counsel (OGC). We evaluated P&SP's processes and controls for conducting investigations to ensure complaints were effectively examined, reported, and resolved. We did not assess the quality of the investigations performed or the results reported.

OIG's 1997 Review of GIPSA's Oversight of Anti-Competitive Practices

Before discussing the findings of our January 2006 audit, I would like to briefly mention the prior work OIG had conducted pertaining to GIPSA, which involved some of the

¹ OIG has conducted both audit and investigative oversight of GIPSA's P&SP programs. While testimony today will focus on recent audit work, I want to also note that we have devoted investigative resources to pursue allegations of fraud and criminal wrongdoing related to GIPSA programs.

same issues. This was followed by a related Government Accountability Office (GAO) report that was issued in September 2000.

In February 1997, OIG issued a report that assessed GIPSA's efforts to monitor and investigate anti-competitive practices. We concluded that GIPSA was not as effective as it could have been in monitoring the livestock procurement market for anti-competitive behavior. Based on this conclusion and the underlying findings, OIG suggested that GIPSA consider several administrative measures to improve its monitoring of the market for anti-competitive behavior, including (1) redistributing the location of its resources by reorganizing the agency's National and Regional Offices, (2) integrating its economics staff into the investigations of anti-competitive practices, and (3) developing procedures to consult with USDA's OGC regarding the initiation and conduct of anti-competitive practice investigations.

In September 2000, GAO released a report on P&SP activities that followed up on our work and reaffirmed our conclusions. GAO provided an update on the actions GIPSA had taken in response to our concerns. Although GIPSA had completed a major restructuring of its Headquarters and field offices in 1999 and had hired staff to strengthen its investigation of alleged anti-competitive practices, GAO reported that two principal factors continued to detract from GIPSA's ability to investigate concerns about anti-competitive practices in these markets. First, GIPSA's investigations were led and conducted primarily by economists without the formal involvement of attorneys from OGC. Second, GIPSA's investigative processes and practices were designed for

traditional trade practice and financial issues that the agency had emphasized for years, and thus were not suited for the more complex anti-competitive practices they needed to address.

Major Findings of OIG's January 2006 Audit of GIPSA's Oversight of P&SP

1. P&SP's Investigative Tracking System

In our January 2006 report, we first found that P&SP's tracking system counted all P&SP activities as "investigations" because there was no policy to better define its activities. The activities that P&SP's tracking system counted as investigations included monitoring publicly available data, sending routine letters to request company-specific information, and performing onsite reviews of companies. OIG found that records in the tracking system were not complete because there were no procedures for validating the accuracy and completeness of information recorded. Consequently, data fields were left blank and the system could not be relied upon as a control for managing P&SP investigations.

According to P&SP data, the agency was tracking a total of 1,842 investigations as of June 30, 2005. The records, however, could not be used to identify the location of work performed (i.e., the P&SP office or the regulated entity's place of business) for 1,799 of the 1,842 investigations. In addition, we found that agency records were incomplete for 973 of the 1,842 investigations mainly because P&SP staff did not record such information as the primary reasons for conducting the investigation, the status of investigative work, and the disposition of closed cases.

We also found that the three P&SP regional offices were not consistently documenting investigative work in the investigative tracking system. Two of the three regional offices classified all activities (i.e., monitoring activities, sending routine correspondence, or performing onsite reviews) as investigations. The Eastern Regional Office was reprimanded on June 14, 2005, for classifying investigations to only include monitoring activities and onsite reviews. The former Deputy Administrator directed each Eastern Regional Office Unit (e.g., competition, trade practice, and financial protection) to devise a strategic plan to address the deficiency in the number of investigations recorded in the investigative tracking system. According to the strategic plans, the units committed to increasing the number of complaints and investigations in the log by adding activities that were previously not included as investigations. These activities included delinquent annual and special reports, bond terminations, bond increases, and registration and bonding. We found this resulted in a significant increase in the number of investigations recorded in the complaints and investigations log. On June 14, 2005, the region was tracking a total of 425 investigations. By comparison, as of September 15, 2005, a total of 760 activities were being tracked by the region. The region climbed from last to first among the three regions by reclassifying over 300 routine activities as investigations.

We recommended that GIPSA implement a policy defining investigations and procedures for recording data in the investigative tracking system. In response, GIPSA issued a policy statement in January 2006, which defined investigations and differentiated between activities to perform onsite reviews from monitoring publicly available data and

requesting company information. GIPSA also agreed to implement procedures by June 2006 for recording data to be tracked and for validating the accuracy and completeness of this data.

2. Management Control over Competition and Complex Investigations

We found that P&SP had established a Senior Management Review Panel (SMRP) to plan and conduct competition and complex investigations. The SMRP was initiated in response to a recommendation from GAO in September 2000. P&SP had agreed to develop a review process for investigations in which complex investigations of anti-competitive activities are subject to review and approval by P&SP Headquarters and OGC. At the time of our review, the panel was comprised of the Deputy Administrator and the Division Directors for Policy and Litigation, Industry Analysis, and Regional Operations. We found that during the period of our audit, the functioning of the SMRP inhibited the agency's ability to investigate anti-competitive activities and unfair trade practices in the livestock and poultry markets. SMRP did not establish an effective process for identifying the work to be performed, approving work plans, performing fieldwork and analysis, and reporting on results. Consequently, no competition and complex investigations were being completed. As of August 29, 2005, all competition and complex investigations, a total of 50, were engaged in the process of being approved by SMRP. Of these 50 investigations, 3 were opened in 2003, and 1 was opened over 3 years ago, in July 2002.

Since P&SP was not performing and completing competition and complex investigations, no referrals were being made to OGC for formal administrative action. In February 2005, P&SP referred one competition investigation to OGC. The most recent referral prior to February 2005 was in November 2002, over 2 years earlier. OGC had not filed any administrative complaints against market participants for anti-competitive practices since 1999 due to the lack of referrals by P&SP.

We recommended that GIPSA implement a well-defined investigative process and a system to effectively communicate management's expectations to staff regarding P&SP's investigative process and specific investigations. GIPSA agreed to implement these recommendations by March 2006. We also recommended that GIPSA implement an organizational structure that appropriately divides responsibility. In January 2006, GIPSA issued a policy statement which described its revised organizational structure to divide responsibility between the Regional Managers and the Deputy Administrator for approving work plans, managing investigations, and reporting results. This should improve GIPSA's ability to complete its investigations.

3. Policy Decisions

We found that due to the flawed control structure that was in place during the period of our review, P&SP was not making policy decisions or evaluating the need for changes in regulations. A new policy group had been created in June 2005; however, P&SP did not establish an internal structure for this group to use to receive, review, and act on policy questions raised by P&SP staff. As a result, timely action was not being taken on issues

that impact the day-to-day business activities of producers and the entities P&SP regulates (e.g., packers, stockyards, and live poultry dealers). We identified 64 policy issues that were awaiting decisions in P&SP Headquarters as of September 30, 2005. These issues covered all types of P&SP investigations (e.g., trade practice, financial protection, and competition) and a variety of topics to be addressed by the Deputy Administrator and the Policy and Litigation Division, such as how to make entries in the system used to track investigations. For 55 of the 64 issues, guidance was requested prior to 2004, with 2 submitted in 2000.

We recommended that GIPSA implement a structure for receiving, reviewing, and acting on policy issues and a process for evaluating the need for regulatory reforms. GIPSA agreed to implement these actions by March 2006.

4. GIPSA's Implementation of Prior OIG and GAO Recommendations

In prior reports, OIG and GAO advised GIPSA on steps P&SP could take to better allocate its resources to monitor the market for anti-competitive behavior. In response, P&SP did take action to reorganize its operations in 1998 and charged the three regional offices with maintaining a high level of expertise in one or more species of livestock. P&SP also assessed its staff's qualifications and hired staff with legal, economic, and statistical backgrounds to strengthen its program operations. In our recent report, however, we found that the agency's actions pertaining to four areas of suggested improvements did not achieve sufficient results. Specifically, P&SP did not (1) effectively integrate economists into investigations, (2) empower the agency's legal

specialist to consult with OGC, (3) hire a manager with experience in leading P&SP investigations, and (4) develop a teamwork approach for investigations with P&SP's economists and OGC's attorneys.

We recommended that GIPSA implement procedures that empower its legal specialists to consult with OGC. In response, GIPSA issued a policy statement in January 2006. We also recommended that the agency implement a process for effectively implementing changes in P&SP operations and establish an internal review function, which GIPSA agreed to do by September 2006.

Conclusion

In summary, we concluded that GIPSA had not established an adequate control structure and environment that allowed the agency to oversee and manage its investigative activities for P&SP. Our review identified material weaknesses in three areas: (1) defining and tracking investigations, (2) planning and conducting competition and complex investigations, and (3) making agency policy. We also found that GIPSA had not taken sufficient actions to strengthen operations in response to findings previously reported by GAO and OIG.

The new leadership at GIPSA has committed to take significant corrective actions to address the issues identified in our report. In January 2006, GIPSA issued policy statements which completed the necessary corrective actions for three of our recommendations. These statements addressed such issues as the agency's definition of

its investigative activities and a revised organizational structure to divide responsibility between the National and Regional Offices for managing the work. GIPSA is working to complete actions on the remaining seven recommendations no later than September 2006. I appreciate the cooperation we received from GIPSA staff throughout the audit and the open manner in which the new Administrator worked with us to address the results of the audit.

This concludes my testimony. Thank you again for inviting me to testify before the Committee and I would be pleased to address any questions you may have.