

May 1993

FINANCIAL AUDIT

Customs Forfeiture Fund's Financial Statements for 1991 and 1990





United States
General Accounting Office
Washington, D.C. 20548

Accounting and Financial
Management Division

B-252847

May 13, 1993

The Honorable Lloyd Bentsen
The Secretary of the Treasury

Dear Mr. Secretary:

This report presents the results of our review of the independent certified public accountants' audits of the Customs Forfeiture Fund's (the Fund) fiscal years 1991 and 1990 financial statements.¹ The Fund accounts for the proceeds that the U.S. Customs Service generates from the forfeiture of property and money as a result of Customs' enforcement of import, export, and drug-related laws. It also accounts for certain costs related to Customs' seizure and forfeiture activities. The auditors did not express an opinion on the fiscal year 1990 financial statements because the Fund's accounting records were incomplete and could not be reconciled due to major internal control problems. In the auditors' opinion, the fiscal year 1991 financial statements were "materially" correct as reported.

KPMG Peat Marwick (KPMG) performed the audits of the Fund's fiscal years 1991 and 1990 financial statements. These audits were required by the Customs and Trade Act of 1990 (Public Law 101-382) (Trade Act). To satisfy our audit responsibilities under the Trade Act, we reviewed the audits done by KPMG to determine if the Congress can rely on the financial statements and the auditors' reports to assess the Fund's financial position. The results of this review will be considered in connection with our ongoing audit of the U.S. Customs Service's fiscal year 1992 financial statements that we elected to perform in accordance with the authority granted by the Chief Financial Officers (CFO) Act of 1990 (Public Law 101-576).

Appendix I of this report contains the auditors' opinion on the financial statements for fiscal year 1991, the Fund's comparative fiscal years 1991 and 1990 financial statements, and the auditors' reports on internal controls and compliance with laws and regulations for fiscal year 1991.

Results in Brief

During our review, we noted a significant problem which we believe adversely impacts the usefulness of the information in the fiscal year 1991 financial statements. We believe that Customs' and KPMG's election to forgo

¹The Fund's financial statements included its statements of financial position, operations, changes in equity, cash flows, and reconciliation to budget reports, as well as the related footnotes.

disclosure in the fiscal year 1991 financial statements of two significant cash items precluded the Congress' and other users' complete understanding of the financial impact that the Fund's internal control problems had on its operations. While recognizing that this is a matter of auditor judgment, if we had been the Fund's auditors, we would have insisted on disclosure of these two cash items.

The Fund's fiscal year 1991 financial statements and related auditors' reports did not disclose that Department of the Treasury's records showed that the Fund had \$6.4 million more in cash than what was recorded in the Fund's accounting records and that neither Customs nor KPMG could determine the reasons for these differences. Also, there was no disclosure that Customs had arbitrarily added a \$10.6 million item, labeled as a "miscellaneous net increase to cash," in order to balance its statement of cash flows and that neither Customs nor KPMG could explain what the amount represented.

KPMG stated that accounting and auditing standards did not require disclosure of these items in the financial statements or the auditors' report thereon, and, in KPMG's judgment, they were not significant enough to warrant disclosure. We disagree with Customs' and KPMG's decision not to disclose these items because stewardship over cash is highly sensitive and critical, especially in the government environment, and we believe that the information is relevant to a reader's appraisal of the financial statements.

We have no other substantive criticisms of the financial statements or the KPMG report thereon or of KPMG's related reports on internal controls and compliance with certain laws and regulations.

Background

In 1984, the Trade and Tariff Act (Public Law 98-573) provided for annual congressional appropriations of up to \$10 million of the net proceeds generated from the forfeiture of monetary instrument seizures and the sale of forfeited seized property to be used to fund certain administrative and enforcement expenses. To account for these proceeds and related expenses, the Trade and Tariff Act established the Fund and authorized Customs to operate it through September 30, 1987.

The Anti-Drug Abuse Act of 1988 (Public Law 100-690) (Drug Act) reestablished the Fund's existence indefinitely. The Drug Act provides for annual congressional appropriations of up to \$20 million of the net proceeds received through the forfeiture activities to be used by Customs

for the payment of discretionary expenses related to these activities. Under the Drug Act, nondiscretionary expenses may be financed through the revenue generated from forfeiture activities without limitation.

Discretionary expenses primarily include purchases of evidence and information related to smuggling of controlled substances; costs of equipment for vessels, vehicles, or aircraft to assist Customs and to enable state and local agencies to assist Customs in law enforcement activities; and reimbursements of costs incurred by state and local law enforcement agencies in joint law enforcement operations. Nondiscretionary expenses primarily include investigative costs and purchases of evidence and information leading to a seizure; costs relating to the warehousing and security of seized and forfeited property; and expenses related to advertising and selling forfeited property.

The Customs and Trade Act of 1990 (Public Law 101-382) required that the Fund's financial statements, starting with those for the fiscal year ending September 30, 1990, be audited annually. Customs contracted with KPMG to perform the audits of the Fund's financial statements for fiscal years ended September 30, 1991 and 1990.

Our review of KPMG's audit is also part of our ongoing fiscal year 1992 financial statement audit of Customs that we elected to perform in accordance with authority granted by the Chief Financial Officers Act of 1990 (Public Law 101-576). Customs is 1 of 10 federal agencies required to prepare financial statements and have them audited as a pilot project under the CFO Act.

These audits play a central role in providing more reliable and complete financial information to the Congress and other users for assessing agencies' financial performance in meeting their mission objectives and in improving the effectiveness of internal controls used to manage programs and safeguard the government's interest. Office of Management and Budget (OMB) Bulletin No. 91-14,² "Audit Requirements for Federal Financial Statements," dated September 10, 1991, established requirements for audits of federal financial statements covering fiscal year 1991 and implemented the audit provisions of the CFO Act. The Fund's September 30, 1991, financial statements were required to be audited in accordance with this Bulletin.

²Office of Management and Budget Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," superseded OMB Bulletin No. 91-14 and became effective on January 8, 1993.

Objective, Scope, and Methodology

Our objective was to determine whether the Congress and other users can rely on the financial statements and auditors' reports to assess the financial position of the Fund.

We conducted our review of KPMG's work in accordance with generally accepted government auditing standards. To determine the reasonableness of KPMG's work and the extent to which we could rely on it, we

- reviewed KPMG's approach and planning of the audit;
- evaluated the qualifications and independence of the audit staff;
- reviewed the Fund's September 30, 1991 and 1990, financial statements and KPMG's reports on its audits of these statements to evaluate compliance with generally accepted accounting principles, required auditing standards,³ and the provisions of OMB Bulletin No. 91-14;
- reviewed and tested KPMG's working papers to determine (1) the nature, timing, and extent of audit work performed, (2) the extent of audit quality control methods KPMG used, (3) whether a study and evaluation was conducted of the Fund's internal control structure, (4) whether KPMG tested transactions for compliance with applicable laws and regulations, and (5) whether the evidence in the working papers supported KPMG's opinion on the financial statements and internal control structure and compliance reports; and
- interviewed top-level KPMG officials that participated in the audit and, as needed, obtained their written response to clarify and resolve questions we had as a result of our review of the fiscal year 1991 financial statements and auditors' reports and related working papers.

Disclosures of Significant Unsupported Balances Were Not Made

Two significant items, \$6.4 million of net differences in cash between Customs' and Treasury's records and \$10.6 million of reported cash provided by operations that could not be accounted for, were not disclosed in the fiscal year 1991 financial statements or the related auditors' report. Customs' inability to identify the specific reasons for these variances increases its vulnerability to waste, fraud, and abuse. These unexplained amounts could have been due to incorrect entries in the accounting records, misappropriation of funds, theft, or a combination of these factors. We believe that Customs' inability to reconcile these items should have been disclosed either in the financial statements or the related auditors' report to enable the Congress and other users to better assess the Fund's financial position and internal controls.

³The required auditing standards consist of generally accepted auditing standards and generally accepted government auditing standards.

**Unreconciled Cash
Balances Not Disclosed**

Customs did not perform reconciliations between its accounting records and its cash accounts maintained by Treasury from inception of the Fund in 1985 to 1991. Treasury regulations and prudent cash management practices require an agency to periodically reconcile its cash balances to Treasury's records. Such reconciliations allow agencies to promptly detect and resolve any differences between agency and Treasury records.

Customs began an extensive effort in 1991 to reconcile cash balances back to 1985. This effort resulted in a net downward adjustment to cash of \$17.3 million. Included in this amount was an increase in cash of \$6.4 million which was not supported by identifiable transactions and was arbitrarily added to make the Fund's accounting records agree with those maintained by Treasury. Customs attributed the \$6.4 million to 1985 activity for which accounting records could not be located. The \$17.3 million of net adjustments was reported in note 4 to the fiscal year 1991 financial statements. However, neither the financial statements nor the auditors' reports disclosed that the records had not been fully reconciled and that \$6.4 million had been arbitrarily added to force the two sets of records into agreement.

Customs and KPMG officials stated that they chose not to disclose the unsupported \$6.4 million because there was no specific accounting or auditing requirement to do so and that such disclosure is a matter of judgment. We disagree with their decision not to disclose the unsupported amount because stewardship over cash assets is highly sensitive and critical in the federal government due to public accountability. While the difference netted to \$6.4 million, included in this total were individual cash transactions that either increased or decreased cash and in aggregate totaled more than the net amount of \$6.4 million. These unresolved differences showed that Customs could not account for all Fund receipts and disbursements nor ensure that information in its accounting records was correct. Customs did not know if these monies were simply incorrectly recorded, misappropriated, or stolen.

The lack of disclosure by Customs and KPMG would have hindered the Congress and other users from understanding the impact of the Fund's poor internal controls over cash management and accounting on its operations. These unresolved differences also demonstrated Customs' inability to maintain responsible stewardship over Fund assets.

Unreconciled Differences in Cash Activity Were Not Reported

Customs arbitrarily increased cash provided by operations by \$10.6 million in the Fund's fiscal year 1991 statement of cash flows because it could not identify all current or prior years' cash transactions. This was 15.4 percent of the total cash provided. The purpose of the statement of cash flows was to explain the net change in cash balances during the year. More specifically, it was to present all significant sources and uses of cash during the fiscal year and to identify the reasons the Fund's cash balance with Treasury changed from the amount that existed as of September 30, 1990, to the amount as of September 30, 1991. KPMG officials stated that KPMG elected not to require Customs to disclose the \$10.6 million as an unidentified amount because KPMG believed that most readers of the financial statements would not understand the unreconciled difference and thereby possibly arrive at erroneous conclusions or draw misleading inferences. Thus, KPMG decided that the disclosure would not enhance the usability of the statements. Also, KPMG officials stated that the situation that led to the unidentified amount was disclosed in KPMG's fiscal year 1990 report on internal controls. In addition, KPMG officials stated that the \$10.6 million unsupported amount was equal to approximately 5 percent of total assets and 4 percent of total revenues and, therefore, was not significant enough to have affected its opinion for the fiscal year 1991 financial statements.

We disagree with KPMG and believe that this item was significant and should have been disclosed to allow a user to better assess the cash flows of the Fund. Although KPMG disclosed major internal control problems with cash in its fiscal year 1990 report on internal controls, KPMG did not specifically explain in its fiscal year 1991 reports that the \$10.6 million unidentified amount was a result of these internal control problems. In addition, while the \$10.6 million represented 5 percent and 4 percent of total assets and total revenues, respectively, it was, as previously noted, 15.4 percent of the reported cash provided by operations. Thus, in our opinion the nature of the item should have been specifically disclosed rather than reported as a "miscellaneous net increase to cash."

Accounting and auditing standards allow an auditor to apply judgment to determine whether a matter is significant enough to warrant disclosure in financial statements. According to the generally accepted government auditing standard on materiality and significance, the auditor should consider materiality in deciding whether a matter requires disclosure in an audit report. One of the criteria to be considered in determining materiality is the monetary value of the item. But, this standard also states that in government audits the materiality level and/or threshold of

acceptable risk may be lower than in similar-type audits in the private sector because of the public accountability of the entity and the visibility and sensitivity of government programs, activities, and functions.

Because of the often subjective nature of judgments about materiality, it is possible for two auditors to differ over what is material. But, in this case, we believe the inability to identify \$10.6 million of cash activity and the need for accountability for cash suggest that the unsupported amount should have been disclosed. The lack of disclosure by Customs and KPMG of this significant unidentified amount precluded financial statement users' complete understanding of the financial impact that the Fund's internal control problems had on its operations. As with the unexplained \$6.4 million adjustment to cash, this unexplained amount is an example of Customs' inability to maintain stewardship over the Fund's assets and highlights the Fund's potential for waste, fraud, and abuse.

Reports on Internal Controls and Compliance With Laws and Regulations

In addition to its opinion report on the Fund's financial statements, KPMG issued reports on the Fund's internal control structure and compliance with laws and regulations.

During our review, we found nothing to indicate that KPMG's reports on the internal control structure were inappropriate. In its 1991 report on internal controls, KPMG identified several material weaknesses in internal controls. The material weaknesses KPMG noted clearly suggest that, while Customs was able to reconstruct the Fund's accounting records to produce year-end financial statements through substantive efforts, accrual basis⁴ financial information reported from its records during the year to the Congress and other users on the Fund's financial position was likely unreliable.

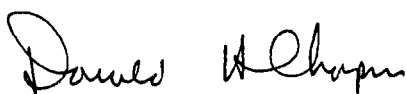
KPMG reported material instances of noncompliance in its 1991 and 1990 reports on compliance with laws and regulations. During our review, we found nothing to indicate that the circumstances reported did not occur.

We are sending copies of this report to the Acting Commissioner of Customs; the Director of the Office of Management and Budget; KPMG Peat Marwick; the Chairmen and Ranking Minority Members of the Senate Committee on Governmental Affairs, the House Committee on Ways and

⁴The accrual basis of accounting involves identifying and recording costs and revenues in the period in which the revenue is earned or the cost incurred rather than in the period revenue is collected or the cost disbursed.

Means, the House Committee on Government Operations, and the Subcommittee on Oversight, House Committee on Ways and Means; and other interested parties. Copies will be made available to others upon request.

Sincerely yours,



Donald H. Chapin
Assistant Comptroller General

Report on Audit of Customs Forfeiture Fund

Overview of Reporting Entity

Overview of the Reporting Entity

In 1984, following recommendations from the General Accounting Office to improve and strengthen the management of seized and forfeited property, Congress passed the Comprehensive Crime Control Act (P.L. 98-473) and the Tariff and Trade Act (P.L. 98-573). These bills authorized the establishment of the Customs Forfeiture Fund as a repository for the deposit of seized currency and net proceeds from the sale of forfeited property. The primary purpose of the Forfeiture Fund was for the payment of unrecovered excess expenses from the sale of seized property.

The Anti-Drug Abuse Act of 1988 (P.L. 100-690) revised the structure and broadened the use of the Forfeiture Fund. As a result of this bill, Customs was authorized to deposit into the Fund all receipts from the sale of forfeited items and all receipts from the forfeiture of seized currency that are not dedicated for asset sharing. From these available receipts, Customs must pay all non-discretionary expenses related to the inventory, storage, maintenance, cartage and sale of seized and forfeited items, including the expenses of the property management contractor. In addition, the Fund now has the authority to incur discretionary costs that are not necessarily associated with seizure actions but that are related to enforcement functions.

The fiscal year 1990 independent auditors' report on internal controls cited specific material weaknesses relating to the agency's Seized Property Program. Subsequently, management developed new policies and procedures which increased oversight of contractor operations and the financial viability of the program. Operating revenue from net sales of forfeited assets and distributed forfeited property increased 61.6 percent in fiscal year 1991 versus fiscal year 1990 while the amount paid to the contractor for managing and selling forfeited assets decreased.

Also, the accuracy of reporting information relating to the Seized Property Program was significantly improved through the nationwide allocation of 75 seized property custodians. Responsibilities of these positions include ensuring timely disposition of property, maintenance and verification of data relating to contractor operations, and review of program operations to ensure compliance with contract requirements.

Appendix I
Report on Audit of Customs Forfeiture Fund

Independent Auditors' Report



Certified Public Accountants

2400 First Indiana Plaza
135 North Pennsylvania Street
Indianapolis, IN 46204-2452

Independent Auditors' Report

United States Customs Service
Washington, D.C.:

We have audited the accompanying statement of financial position (statutory basis) of the Customs Forfeiture Fund (Fund), as of September 30, 1991, and the related statements of operations, changes in equity, cash flows and reconciliation to budget report (statutory basis) for the year then ended. These financial statements are the responsibility of the management of the Fund. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our 1991 audit in accordance with generally accepted auditing standards, Government Auditing Standards, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin 91-14, "Audit Requirements for Federal Financial Statements." Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our 1991 audit provides a reasonable basis for our opinion.

Accounting principles for Federal entities are currently being studied by the Federal Accounting Standards Advisory Board. Accounting principles for Federal entities are to be promulgated by the Comptroller General and the Director of the Office of Management and Budget, based on advice from the Board. In the interim, Federal agencies have been advised to follow the applicable accounting principles contained in agency accounting policy, procedures manuals, and/or related guidance. The summary of significant accounting policies included in the notes to financial statements describes the accounting principles prescribed by the Fund and used to prepare the financial statements which is a comprehensive basis of accounting other than generally accepted accounting principles. Note 1 also discloses the differences between these accounting principles and Title 2 of General Accounting Office's Policy and Procedures Manual for Guidance of Federal Agencies.

In our opinion, the 1991 financial statements referred to above present fairly, in all material respects, the financial position (statutory basis) of the Fund as of September 30, 1991, and the results of its operations, cash flows and reconciliation to budget report (statutory basis) for the year then ended on the basis of accounting described in Note 1.

Appendix I
Report on Audit of Customs Forfeiture Fund

Peat Marwick

United States Customs Service
Washington, D.C.

We were engaged to audit the accompanying statement of financial position of the Fund as of September 30, 1990, and the related statements of operations, changes in equity, cash flows and reconciliation to budget reports for the year then ended. These financial statements are the responsibility of the management of the Fund.

We were unable to satisfy ourselves regarding the 1990 amounts discussed in this and the three succeeding paragraphs of this report. We did not observe the physical quantities of the inventory of forfeited assets as of September 30, 1990 (stated at \$5,241,000) because that date was prior to the time we were appointed auditors for the Fund. The balance of inventory of forfeited assets also affects the balance of deferred revenue from forfeited assets and affects the results of operations and cash flows for the year ended September 30, 1990.

We were unable to obtain documentation to determine whether the mortgages and claims payable balance at September 30, 1990 (stated at \$1,296,000) includes all such liabilities of the Fund. The Fund's 1990 accounting records do not provide sufficient detail to identify forfeited inventory with the associated mortgage or claim. The balance of mortgages and claims payable enters into the calculation of the distribution payable to the U.S. Treasury and affects the results of operations and cash flows for the year ended September 30, 1990.

We were unable to obtain documentation to determine whether revenue from forfeited currency and monetary instruments (stated at \$58,362,000), payments in lieu of forfeiture and reimbursed storage costs (stated at \$22,629,000) and revenue from distributed forfeited assets (stated at \$45,296,000) includes all such revenue which should be recognized for the year ended September 30, 1990. The Fund's 1990 accounting records do not provide sufficient information to identify, for the year ended September 30, 1990, all forfeited currency and monetary instruments, payments in lieu of forfeiture and reimbursed storage costs nor all revenue from distributed forfeited assets.

Prior to September 30, 1990, the Fund was not required to prepare financial statements in accordance with generally accepted accounting principles. Accordingly, the statement of financial position of the Fund as of September 30, 1989 was not audited. Statement of financial position amounts as of September 30, 1989 enter into the determination of revenue, expenses, distributions and cash flows for the year ended September 30, 1990.

In our report dated March 1, 1991, we did not express an opinion on the 1990 financial statements because, in part, we were unable to obtain documentation to support whether the balance recorded for cash at U.S. Treasury at September 30, 1990 was fairly presented. During 1991, management was able to present documentation to support that balance. We have applied auditing procedures to such documentation, and, accordingly the lack of sufficient documentation to support the balance of cash at the U.S. Treasury at September 30, 1990 no longer affects our report on the 1990 financial statements.

Appendix I
Report on Audit of Customs Forfeiture Fund

~~KPMG~~ Peat Marwick

United States Customs Service
Washington, D.C.

As discussed in note 1 to the financial statements, the Fund carries its inventory of forfeited assets at September 30, 1990 at values which were subjectively estimated by Customs officials at the time the related seizures took place. These estimated values are not the result of independent valuation procedures. Correspondingly, property transferred to other Federal agencies, deferred revenue from forfeited assets, and distributions payable during the year ended September 30, 1990 are recorded on the basis of such values. Forfeited assets should be stated at net realizable value. The effects of not stating forfeited assets at net realizable value are not reasonably determinable.

Because of the matters discussed in paragraphs six through nine of this report, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements as of, and for the year ended September 30, 1990.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. Supplemental schedules 1 and 2, "Analysis of Revenue and Expenses and Distributions" (as discussed in Note 5), are not a required part of the basic financial statements of the Fund, but is supplementary information required by the 1990 Customs and Trade Act, Subtitle C, Section 121. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

The financial information presented in management's fiscal year 1991 Overview of the Reporting Entity and Supplemental Financial and Management Information is not a required part of the basic financial statements but is supplementary information required by OMB Bulletin No. 91-15, "Guidance on Form and Content of Financial Statements on FY 1991 Financial Activity." We have applied certain limited procedures to the information, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it. This information is addressed, however, in our auditors' report on compliance in accordance with Section 6.a (3), (4) and (5) of OMB Bulletin No. 91-14.

This report is intended for the information of the Congress, the U.S. General Accounting Office, the management of the Fund and the U.S. Customs Service. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

KPMG Peat Marwick

December 31, 1991

**Appendix I
Report on Audit of Customs Forfeiture Fund**

Statements of Financial Position

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Statements of Financial Position
(Statutory Basis)

September 30, 1991 and 1990

(Dollars in thousands)

<u>Assets</u>	<u>1991</u>	<u>1990</u> (As restated)
Current assets:		
Cash at U.S. Treasury (note 4)	\$ 96,919	61,744
Accounts receivable:		
Other U.S. Customs funds (note 4)	59,615	25,631
Other Federal agencies	-	9,195
Contractors (note 4)	1,059	5,151
Other	<u>75</u>	<u>-</u>
	60,749	39,977
Investigative and travel advances receivable	<u>21,121</u>	<u>2,686</u>
Inventory of forfeited assets (note 2):		
Held for sale	25,903	4,148
To be shared with federal, state or local agencies	<u>2,232</u>	<u>1,093</u>
	<u>28,135</u>	<u>5,241</u>
	\$ <u>206,924</u>	<u>109,648</u>
 <u>Liabilities and Equity of U.S. Government</u>		
Current liabilities:		
Accounts payable:		
Contractors	2,093	4,797
Other (note 4)	<u>1,613</u>	<u>1,369</u>
	<u>3,706</u>	<u>6,166</u>
Mortgages and claims payable	<u>769</u>	<u>1,296</u>
Distributions payable:		
To state and local agencies	34,442	10,160
To other Federal agencies	2,624	-
To foreign countries	218	6,130
To U.S. Treasury (note 4)	<u>110,235</u>	<u>52,065</u>
	<u>147,519</u>	<u>68,355</u>
Deferred revenue from forfeited assets (note 4)	<u>25,134</u>	<u>2,852</u>
Total current liabilities	<u>177,128</u>	<u>78,669</u>
Equity of U.S. Government:		
Retained earnings - statutory carryover	15,000	15,000
Unliquidated obligations	<u>14,796</u>	<u>15,979</u>
Total equity of U.S. Government	<u>29,796</u>	<u>30,979</u>
	\$ <u>206,924</u>	<u>109,648</u>

See accompanying notes to financial statements.

**Appendix I
Report on Audit of Customs Forfeiture Fund**

Statements of Operations

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

**Statements of Operations
(Statutory Basis)**

For the years ended September 30, 1991 and 1990

(Dollars in thousands)

	1991	1990
Operating revenue:		
Undistributed forfeited currency and monetary instruments	\$ 97,926	58,362
Distributed forfeited assets:		
Currency	92,645	39,880
Property	17,596	5,416
Sales of forfeited assets (note 2)	12,031	13,857
Less: Mortgages and claims against forfeited assets	<u>(1,824)</u>	<u>(2,066)</u>
Net sales of forfeited assets	10,207	11,791
Payments in lieu of forfeiture and reimbursed storage costs (net of refunds of \$1,402 and \$2,176, respectively)	19,173	22,629
Miscellaneous income	<u>578</u>	<u>-</u>
	<u>238,125</u>	<u>138,078</u>
Operating expenses:		
Non-discretionary expenses:		
Contractor and selling	18,592	18,630
Payroll costs	1,826	-
Purchases of evidence and information leading to seizures	12,287	2,763
Other case related	<u>3,895</u>	<u>1,702</u>
	<u>36,600</u>	<u>23,095</u>
Discretionary expenses:		
Other purchases of evidence and information	1,081	7,672
Specialized contract services	1,749	1,543
Joint operations	2,340	902
Other program management	20	1,245
Property purchased with forfeited currency and transferred to other U.S. Customs fund (note 3)	<u>5,942</u>	<u>-</u>
	<u>11,132</u>	<u>11,362</u>
Total operating expenses	<u>47,732</u>	<u>34,457</u>
Excess of operating revenue over operating expenses	190,393	103,621
Interest expense	<u>6</u>	<u>62</u>
Excess of revenue over expenses	<u>190,387</u>	<u>103,559</u>
Distributions of forfeited assets:		
Assets shared with state and local agencies	95,205	35,616
Currency shared with foreign countries	245	6,130
Assets shared with other Federal agencies	<u>14,791</u>	<u>3,550</u>
	<u>110,241</u>	<u>45,296</u>
Excess of revenue over expenses and distributions	\$ <u>80,146</u>	<u>58,263</u>

See accompanying notes to financial statements.

Appendix I
Report on Audit of Customs Forfeiture Fund

Statements of Changes in Equity

CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE
Statements of Changes in Equity
(Statutory Basis)

For the years ended September 30, 1991 and 1990

(Dollars in thousands)

	Retained earnings - statutory carryover	Unliquidated obligations	Total
Unadjusted balance as of September 30, 1989 (unaudited)	\$ 11,293	13,891	25,184
Prior period adjustments to present financial statements on the accrual basis and correct accounting errors	<u>17,781</u>	<u>(4,701)</u>	<u>13,080</u>
Adjusted balance as of September 30, 1989 (unaudited)	29,074	9,190	38,264
Net increase in obligation of current resources	(6,789)	6,789	-
Excess of revenue over expenses and distributions	58,263	-	58,263
Addition to distribution payable to U.S. Treasury	<u>(65,548)</u>	<u>-</u>	<u>(65,548)</u>
Balance as of September 30, 1990	15,000	15,979	30,979
Net decrease in obligation of current resources	1,183	(1,183)	-
Excess of revenue over expenses and distributions	80,146	-	80,146
Addition to distribution payable to U.S. Treasury	<u>(81,329)</u>	<u>-</u>	<u>(81,329)</u>
	\$ <u>15,000</u>	<u>14,796</u>	<u>29,796</u>

See accompanying notes to financial statements.

**Appendix I
Report on Audit of Customs Forfeiture Fund**

Statements of Cash Flows

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Statements of Cash Flows
(Statutory Basis)

For the years ended September 30, 1991 and 1990

(Dollars in thousands)

	1991.	1990 (As restated)
Cash flows from operating activities:		
Excess of revenue over expenses and distributions	\$ 80,146	58,263
Adjustments to reconcile excess of revenue over expenses and distributions to net cash provided by operating activities:		
Increase in accounts receivable from other U.S. Customs funds	(33,984)	(6,947)
Decrease (increase) in accounts receivable from other Federal agencies	9,195	(9,195)
Decrease (increase) in accounts receivable from contractors	4,092	(4,021)
Increase in investigative and travel advances receivable	(18,435)	(153)
Decrease in accounts payable to contractors	(2,704)	(3)
Increase in other accounts payable	244	1,369
Increase in distributions payable	20,994	13,110
Increase (decrease) in other, net	<u>9,378</u>	<u>(1,570)</u>
Net cash provided by operating activities	<u>68,926</u>	<u>50,853</u>
Cash used in financing activities:		
Distribution paid to U.S. Treasury	<u>33,751</u>	<u>68,022</u>
Cash used in financing activities	<u>33,751</u>	<u>68,022</u>
Net increase (decrease) in cash at U.S. Treasury	35,175	(17,169)
Cash at U.S. Treasury at beginning of year, as previously reported	-	96,214
Adjustments to cash (note 4)	-	(17,301)
Cash at U.S. Treasury at beginning of year, as restated	<u>61,744</u>	-
Cash at U.S. Treasury at end of year	\$ <u>96,919</u>	<u>61,744</u>

Inventory forfeited of \$18 million and \$5 million was shared with state or local agencies or transferred to other Federal agencies during the year ended September 30, 1991 and 1990, respectively.

See accompanying notes to financial statements.

**Appendix I
Report on Audit of Customs Forfeiture Fund**

Statements of Reconciliation to Budget Reports

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Statements of Reconciliation to Budget Reports
(Statutory Basis)

For the years ended September 30, 1991 and 1990

(Dollars in thousands)

	<u>1991</u>	<u>1990</u> (As restated)
Increases (decreases) in outlays:		
Total expenses and distributions	\$ 157,979	79,815
Net reversals of prior year payables and additional current year payables	17,944	(13,969)
Transaction excluded from expenses and distributions:		
Distribution to U.S. Treasury	-	68,022
Distributions not requiring outlays:		
Property transferred to other Federal agencies and to state or local agencies	(17,596)	(5,416)
Cash disbursements for mortgages, claims and refunds	4,035	4,242
Subsequent adjustments	9,865	2,053
Other, net	<u>520</u>	<u>3,532</u>
 Outlays as reported in budget reports	 \$ <u>172,747</u>	 <u>138,279</u>

See accompanying notes to financial statements

Appendix I
Report on Audit of Customs Forfeiture Fund

Notes to Financial Statements

CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE

Notes to Financial Statements
(Statutory Basis)

September 30, 1991 and 1990

(1) The Fund and Summary of Significant Accounting Policies

(a) The Fund

The Tariff and Trade Act (the Act) was signed into law on October 12, 1984. The Act authorized the United States Customs Service (Customs) to utilize the net proceeds it generates from the forfeiture of monetary instruments seizures and the sale of forfeited seized property to fund certain administrative and enforcement expenses. The Act established the Customs Forfeiture Fund (the Fund) within Customs to account for these net proceeds and related expenses. The Act established the Fund to be in operation through September 30, 1987. In 1988, the Anti-Drug Abuse Act (Drug Act) reestablished the Fund and authorized its continuance indefinitely. The primary objectives of the forfeiture program are to (1) reduce the economic power of criminals and their enterprises, (2) improve intergovernmental cooperation by sharing proceeds with state and local governments and (3) generate revenues to help fight the war on drugs.

Under the 1930 Tariff Act and later amendments, Customs enforces importing and exporting and drug-related laws of the United States. Accordingly, when violations are discovered, Customs has the authority to immediately seize the possessions of the violator. The seized property or currency may eventually be returned to the violator if the violation is cured or otherwise dismissed. Also, Customs may return the property to the violator if the violator accepts Customs' terms for a mitigated seizure and, accordingly, makes a payment in lieu of forfeiture. However, if the possessions are not returned to the violator, the property is forfeited to Customs through either administrative or judicial procedures. Once forfeited, the property and currency are either retained for official use of Customs, destroyed, sold, or transferred to another state, local, or Federal agency or foreign country.

Under the Drug Act, the Fund is available for the payment of certain discretionary and non-discretionary expenses. Non-discretionary expenses include all proper expenses of the seizure (including investigative costs and purchases of evidence and information leading to seizure, holding costs, security costs, etc.), awards of compensation to informers, satisfaction of liens against the forfeited property, and claims of parties in interest to forfeited property. Discretionary expenses include purchases of evidence and information related to smuggling of controlled substances, equipment to enable Customs', state or local agencies' vessels, vehicles or aircraft to assist in law enforcement activities, reimbursement of private persons for expenses incurred while cooperating with Customs in investigations, reimbursements of costs incurred by State and local law enforcement agencies in joint law enforcement operations with Customs and publication of the availability of awards.

Appendix I
Report on Audit of Customs Forfeiture Fund

CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE

Notes to Financial Statements
(Statutory Basis)

Discretionary expenses are subject to an annual Congressional appropriation. Congress has authorized that up to \$20 million of the proceeds received through the forfeiture activities may be used for the payment of discretionary expenses. For the year ended September 30, 1991, \$14,855,000 was appropriated by Congress for these purposes. Under the Drug Act, non-discretionary expenses may be financed through the revenue generated from forfeiture activities without limitation.

At the end of each fiscal year, unobligated amounts in excess of \$15 million remaining in the Fund are to be returned to the general fund of the Treasury of the United States. The unobligated amount is determined to be total current assets less total current liabilities (excluding distribution payable to U.S. Treasury) and less unliquidated obligations. As of September 30, 1991 and 1990, unobligated amounts of \$125 million and \$67 million, respectively, remained in the Fund. Accordingly, a liability of \$110 million and \$52 million to the U.S. Treasury has been recognized in the accompanying statement of financial position. Distribution payable to U.S. Treasury has been recognized in the accompanying statement of changes in equity. The actual amount returned to the U.S. Treasury is determined on a cash basis.

The Fund maintains a contract with an unrelated entity whereby the other entity holds seized property on consignment. Upon forfeiture, the contractor conducts auction sales on behalf of Customs and collects sale proceeds from purchaser and remits to the Fund. For assets remitted, the contractor collects reimbursements from violators for asset management expenses incurred.

The Fund is a component unit of Customs and as such, employees of Customs perform certain operational and administrative tasks related to the Fund. Beginning in fiscal year 1991, based on an opinion received from Customs' legal counsel, payroll costs of employees directly involved in the security and maintenance of forfeited property are included in the financial statements of the Fund. Also based on this legal opinion, indirect payroll costs of Customs' employees who work part of their work day on Fund activities should not be charged to the Fund.

(b) Summary of Significant Accounting Policies

Basis of Presentation

The Fund's financial statements present all accounts related to Customs' forfeiture activities on the accrual basis. There are no significant differences between the policies followed by the Fund and the policies required by Title 2 of the United States General Accounting Office's Policy and Procedures Manual for Guidance of Federal Agencies, except as described in note 3. The Fund is a revolving fund, which is the type of fund used by Federal agencies to account for business-type operations. Accordingly, revenue and expense amounts are closed into retained earnings - statutory carryover at the end of the fiscal year.

Appendix I
Report on Audit of Customs Forfeiture Fund

CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE

Notes to Financial Statements
(Statutory Basis)

Cash at U.S. Treasury

The Fund maintains cash in the U.S. Treasury. Such monies are available to pay current liabilities and finance authorized purchase commitments.

Inventory of Forfeited Assets

For fiscal year 1991, the inventory of forfeited assets is recorded at estimated net realizable value based on historical sales experiences. Direct and indirect holding costs are not capitalized for individual forfeited assets. Forfeited currency is reflected as cash at U.S. Treasury in the accompanying statement of financial position. Seized property and currency are not legally owned by Customs until forfeiture and accordingly are not reflected in the accompanying financial statements. For fiscal year 1990, the inventory of forfeited assets is recorded at a value estimated by Customs and contractor officials. The 1990 value is not based on independent valuation procedures, and as such, does not represent the net realizable value.

Investigative and Travel Advances

Investigative and travel advances represent monies advanced to agents for use in conducting investigative operations (i.e., flash rolls) and payments to informants. Advances are reflected in the Fund when the monies are provided to the agents. An expense is recognized in the Fund when the payment to the informant is made. Prior to fiscal year 1991, advances for payments to informants were not reflected in the financial statements until the actual informant was paid.

Revenue Recognition

Revenue from the forfeiture of property is deferred until such property is sold or transferred to a state, local or Federal agency or foreign government. Sales of forfeited inventory are final. Revenue is not recorded if the forfeited asset is ultimately destroyed.

Revenue from currency is recognized upon forfeiture. Payments in lieu of forfeiture (e.g., mitigated seizures) are recognized as revenue when the payment is received, because the earnings process is complete.

Appendix I
Report on Audit of Customs Forfeiture Fund

CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE

Notes to Financial Statements
(Statutory Basis)

Assets Shared or Transferred

Forfeited property or currency may be shared with Federal, state or local agencies or foreign countries who provide direct or indirect assistance in the related seizure. Beginning in fiscal year 1991, proceeds from sale of forfeited property may also be shared with state or local agencies. In addition, the Fund may transfer any forfeited property to another Federal agency (including other Customs funds) which would benefit from the use of the item. Upon proper approval to share or transfer the asset, revenue from distributed forfeited assets and distributions are recognized for the recorded value of the asset to be shared or transferred thereby resulting in no gain or loss recognized.

Mortgages and Claims Payable

Mortgages and claims on forfeited assets (except vessels and real property) are recognized as a liability and a reduction of deferred revenue from forfeited assets when the asset is forfeited. To the extent of proceeds received, the Fund pays the related mortgage or claim when the asset is sold. The payment of mortgages and claims are shown as a reduction of sales. Mortgages on vessels and real property are paid when the related asset is forfeited.

Equity of U.S. Government

Unliquidated obligations represent the amount of undelivered purchase orders and contracts which have been obligated with current resources. A liability is recognized and correspondingly the unliquidated obligation is reduced as goods are received or services are performed.

Retained earnings are the unobligated statutory amount allowed to be retained by the Fund under the Drug Act.

Tax Status

The Fund, as part of Customs which is a Federal agency, is not subject to Federal, state or local income taxes.

Statements of Reconciliation to Budget Reports

The accompanying statements of reconciliation to budget reports reconciles total expenses and distributions as reported in the accompanying statements of operations with outlays as reported in the Office of Management and Budget Report, SF-133, "Report on Budget Execution" for the years ended September 30, 1991 and 1990. In fiscal year 1990, the Fund reflected outlays on two separate SF-133 reports which, when combined, represent total outlays of the Fund.

**Appendix I
Report on Audit of Customs Forfeiture Fund**

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Notes to Financial Statements
(Statutory Basis)

(2) Inventory of Forfeited Assets

Inventory of forfeited assets consists of the following as of September 30, 1991 and 1990 (dollars in thousands):

	<u>1991</u>	<u>1990</u>
General property	\$ 20,321	2,175
Real property	6,314	508
Vessels	267	928
Aircraft	617	911
Vehicles	<u>616</u>	<u>719</u>
	\$ <u>28,135</u>	<u>5,241</u>

As of September 30, 1991, 97% of the inventory of forfeited assets was held by the outside contractor discussed in Note 1. The remaining inventory was held by Customs.

Total seized currency, which is not included in the accompanying financial statements, is \$459 million (unaudited) and \$214 million (unaudited) as of September 30, 1991 and 1990, respectively, of which \$338 million (unaudited) and \$66 million (unaudited) is evidentiary, respectively. Total seized property, which is also not included in the accompanying financial statements, is valued at \$545 million (unaudited) and \$147 million (unaudited) as of September 30, 1991 and 1990, respectively.

The following schedule summarizes sales of forfeited inventory by category for the year ended September 30, 1991 and 1990 (dollars in thousands):

	<u>1991</u>	<u>1990</u>
General property	\$ 4,670	4,792
Real property	502	2,188
Vessels	3,182	1,830
Aircraft	891	2,109
Vehicles	<u>2,786</u>	<u>2,938</u>
	\$ <u>12,031</u>	<u>13,857</u>

The estimated value of destroyed forfeited inventory was approximately \$24 million (unaudited) and \$20 million (unaudited) for the years ended September 30, 1991 and 1990, respectively. This estimated value is as determined by Customs and contractor officials. Property destroyed primarily consisted of general property, such as illegal weapons and counterfeit merchandise.

**Appendix I
Report on Audit of Customs Forfeiture Fund**

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Notes to Financial Statements
(Statutory Basis)

(3) Related Party Transactions

Certain capital assets of Customs, such as communication equipment and conveyances, are utilized at times for the Fund's activities. These assets are capitalized in another fund within Customs. During the year \$5,942,000 of capital assets purchased with forfeited currency were transferred to that other fund within Customs and are shown as discretionary expenses in the accompanying financial statements. This accounting treatment differs from Title 2 in that Title 2 requires these expenditures to be capitalized in the Fund.

(4) Adjustments to Beginning of Year Balances

The fiscal year 1990 balances have been restated to reflect the correction of errors in the recording of cash, accounts receivable, accounts payable, deferred revenue and distribution payable to U.S. Treasury in prior years. As a result, beginning of the year balances have been adjusted from those previously reported as follows (dollars in thousands):

Cash at U.S. Treasury, as previously reported	\$ 79,045
Net adjustment to reconcile cash balance to U.S. Treasury	(17,301)
Cash at U.S. Treasury, as restated	\$ <u>61,744</u>
Accounts receivable - other U.S. Customs funds, as previously reported	\$ 24,477
Additional accounts receivable	<u>1,154</u>
Accounts receivable - other U.S. Customs funds, as restated	\$ <u>25,631</u>
Accounts receivable - contractors, as previously reported	\$ 3,568
Additional accounts receivable	<u>1,583</u>
Accounts receivable - contractors, as restated	\$ <u>5,151</u>
Accounts payable - other, as previously reported	\$ 1,154
Additional accounts payable	<u>215</u>
Accounts payable - other, as restated	\$ <u>1,369</u>
Deferred revenue from forfeited assets, as previously reported	\$ 4,148
Reduction of deferred revenue	(1,296)
Deferred revenue from forfeited assets, as restated	\$ <u>2,852</u>
Distributions payable to U.S. Treasury, as previously reported	\$ 65,548
Net impact of restatements	(13,483)
Distributions payable to U.S. Treasury, as restated	\$ <u>52,065</u>

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Report on Audit of Customs Forfeiture Fund

CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE

Notes to Financial Statements
(Statutory Basis)

The equity balance is established by law, with any unobligated amounts returned to the general fund of the Treasury of the United States. Accordingly, adjustments to previous year's balances impact Distributions Payable to U.S. Treasury.

The impact of the above adjustments on amounts previously reported in the statement of operations can not be determined.

(5) Analysis of Revenue and Expenses and Distributions

The supplemental schedule "Analysis of Revenue and Expenses and Distributions" is required under the 1990 Customs and Trade Act, Subtitle C, Section 121. The amounts in the schedule were determined from information obtained from a Customs' information system. This system maintains revenue and expenses by each seizure for property held at the contractor. The percentages of revenue and expenses from this system were applied to revenue and expenses and distributions as reflected in the accompanying statements of operations. Because Customs does not have a cost accounting system for the Fund, the method used does not provide reliable information in the analysis of revenue and expenses and distributions by type of disposition. For example, the Fund does not earn a profit on reimbursed storage costs, although the schedule shows otherwise. The information is presented to comply with the requirements of the Customs and Trade Act.

**Appendix I
Report on Audit of Customs Forfeiture Fund**

Supplemental Schedules

Supplemental Schedule 1

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Analysis of Revenue and Expenses and Distributions

For the year ended September 30, 1991

(Dollars in thousands)

Revenue and expenses and distributions by asset category (note 5):

	<u>Revenue</u>	<u>Expenses and Distributions</u>
Vehicles	\$ 13,376	17,812
Vessels	10,303	12,690
Aircraft	3,159	2,379
General property	23,049	34,630
Real property	893	1,049
Currency and monetary instruments	<u>190,571</u>	<u>92,645</u>
	241,351	161,205
Less:		
Mortgages and claims	(1,824)	(1,824)
Refunds	<u>(1,402)</u>	<u>(1,402)</u>
	\$ <u>238,125</u>	<u>157,979</u>

Revenue and expenses and distributions by type of disposition (note 5):

	<u>Revenue</u>	<u>Expenses and Distributions</u>
Sales (including forfeited currency and monetary instruments)	\$ 111,539	15,950
Reimbursed storage costs	8,188	3,470
Placed into official use of other		
Customs funds	3,411	3,726
Assets shared with state and local agencies	95,205	95,864
Destructions	962	1,275
Cancellations (including payments in lieu of forfeiture)	10,421	1,392
Assets shared with other Federal agencies	11,380	11,681
Assets shared with foreign countries	245	245
Pending disposition	<u>-</u>	<u>27,602</u>
	241,351	161,205
Less:		
Mortgages and claims	(1,824)	(1,824)
Refunds	<u>(1,402)</u>	<u>(1,402)</u>
	\$ <u>238,125</u>	<u>157,979</u>

**Appendix I
Report on Audit of Customs Forfeiture Fund**

Supplemental Schedules

Supplemental Schedule 2

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Analysis of Revenue and Expenses and Distributions

For the year ended September 30, 1990

(Dollars in thousands)

Revenue and expenses and distributions by asset category (note 5):

	Revenue	Expenses and Distributions
Vehicles	\$ 9,877	11,398
Vessels	6,614	9,276
Aircraft	6,173	2,430
General property	16,138	20,189
Real property	5,291	884
Currency and monetary instruments	<u>98,227</u>	<u>39,880</u>
	142,320	84,057
Less:		
Mortgages and claims	(2,066)	(2,066)
Refunds	<u>(2,176)</u>	<u>(2,176)</u>
	\$ <u>138,078</u>	<u>79,815</u>

Revenue and expenses and distributions by type of disposition (note 5):

	Revenue	Expenses and Distributions
Sales (including forfeited currency and monetary instruments)	\$ 71,665	18,157
Reimbursed storage costs	9,103	6,289
Placed into official use of other		
Customs funds	2,000	2,708
Assets shared with state and local agencies	35,616	36,479
Destructions	554	3,262
Cancellations (including payments in lieu of forfeiture)	15,702	2,503
Assets shared with other Federal agencies	1,550	2,019
Assets shared with foreign countries	6,130	6,130
Pending disposition	<u>-</u>	<u>6,510</u>
	142,320	84,057
Less:		
Mortgages and claims	(2,066)	(2,066)
Refunds	<u>(2,176)</u>	<u>(2,176)</u>
	\$ <u>138,078</u>	<u>79,815</u>

Appendix I
Report on Audit of Customs Forfeiture Fund

Independent Auditors' Report on Compliance



Certified Public Accountants

2400 First Indiana Plaza
135 North Pennsylvania Street
Indianapolis, IN 46204-2452

Independent Auditors' Report on Compliance

United States Customs Service
Washington, D.C.:

We have audited the financial statements of the Customs Forfeiture Fund (the Fund) as of and for the year ended September 30, 1991 and have issued our report thereon dated December 31, 1991.

We conducted our audit in accordance with generally accepted auditing standards, Government Auditing Standards, issued by the Comptroller General of the United States, and the Office of Management and Budget (OMB) 91-14, "Audit Requirements for Federal Financial Statements." Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws and regulations applicable to the Fund is the responsibility of the management of the Fund. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we tested compliance with certain provisions of laws and regulations that may directly affect the financial statements including the Budget and Accounting Procedures Act of 1950; Antideficiency Act; Federal Managers' Financial Integrity Act of 1982; Prompt Payment Act; and Chief Financial Officers Act of 1990 identified by OMB and the Anti-Drug Abuse Act; Trade and Traffic Act; 19 USC 1500 Series; 19 USC 1600 Series; 18 USC 981; and Comprehensive Crime Control Act which have been identified by the Fund. As part of our audit, we applied procedures to management's process for evaluating and reporting on internal control and accounting systems as required by the Federal Managers' Financial Integrity Act (FMFIA) and compared the agency's most recent FMFIA reports with the evaluation we conducted of the entity's internal control system. We also reviewed and tested the entity's policies, procedures, and systems for documenting and supporting financial, statistical, and other information presented in management's Overview of the Reporting Entity and Supplemental Financial and Management Information. However, our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

Material instances of noncompliance are failures to follow requirements, or violations of prohibitions, contained in laws or regulations that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the financial statements. The results of our tests of compliance disclosed the following material instances of noncompliance, the effects of which have been corrected in the Fund's 1991 financial statements.

Appendix I
Report on Audit of Customs Forfeiture Fund

 Peat Marwick

United States Customs Service
Washington, D.C.

U.S. Customs does not maintain the accounts of the Fund in accordance with Title 2 of the United States General Accounting Office's Policy and Procedures Manual for Guidance of Federal Agencies. Title 2, which was adopted by the Fund, requires Federal agencies to maintain accounts of the agency on the accrual basis. The cash basis of accounting may be followed if the differences between the results of cash and accrual accounting are insignificant. U.S. Customs maintains its general ledger system for the Fund on a cash basis, which differs significantly from the accrual basis.

The Fund's internal control structure does not comply with the Budget and Accounting Procedures Act, Section 3512, "Executive Agency's Accounting System." This Act requires Federal agencies to establish an internal control structure which ensures the safeguarding of assets and the proper recording of revenues and expenditures. The Fund's internal control structure has certain material weaknesses as described in our Report on Internal Controls dated December 31, 1991, which cause noncompliance with this Act.

The Fund is not in compliance with 19 USC 1613 b(d) which requires investment of amounts not currently needed for operation of the Fund in obligations of, or guaranteed by, the United States. Based on our discussions with management this is due to Customs not being able to determine the amount of excess funds as the accounting system does not identify excess forfeited receipts available for investments. We recommend the Fund implement procedures to account for excess receipts on a periodic basis throughout the year in order to invest the excess money as required.

We considered these material instances of noncompliance in forming our opinion on whether the Fund's 1991 financial statements are presented fairly, in all material respects, in conformity with the applicable accounting principles described in Note 1 to the financial statements, and this report does not affect our report dated December 31, 1991 on those financial statements.

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, the Fund complied, in all material respects, with the provisions referred to in the third paragraph of this report, and with respect to the items not tested, nothing came to our attention that caused us to believe that the Fund had not complied, in all material respects, with those provisions.

Appendix I
Report on Audit of Customs Forfeiture Fund

Peat Marwick

United States Customs Service
Washington, D.C.

This report is intended for the information of the Congress, the U.S. General Accounting Office, the management of the Fund and the U.S. Customs Service. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

KPMG Peat Marwick

December 31, 1991

Appendix I
Report on Audit of Customs Forfeiture Fund

Independent Auditors' Report on Internal Controls



Certified Public Accountants

2400 First Indiana Plaza
135 North Pennsylvania Street
Indianapolis, IN 46204-2452

Independent Auditors' Report on Internal Controls

United States Customs Service
Washington, D.C.:

We have audited the financial statements of the Customs Forfeiture Fund (the Fund) as of and for the year ended September 30, 1991, and have issued our report thereon dated December 31, 1991.

We conducted our audit in accordance with generally accepted auditing standards, Government Auditing Standards, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin 91-14 "Audit Requirements for Federal Financial Statements." Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing our audit of the Customs Forfeiture Fund financial statements for the year ended September 30, 1991, we considered its internal control structure. The purposes of this consideration were to: (i) determine our auditing procedures for the purpose of expressing our opinion on the financial statements; and (ii) determine whether the internal control structure meets the objectives identified in the following paragraph. This included obtaining an understanding of the internal control policies and procedures and assessing the level of control risk relevant to all significant cycles, classes of transactions, or account balances.

The management of the Fund is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that obligations and costs are in compliance with applicable laws; funds, property, and other assets are safeguarded against loss, unauthorized use, or misappropriation; and revenues and expenditures applicable to agency operations are properly recorded to permit the preparation of financial statements in accordance with the accounting principles described in Note 1 to the financial statements. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Appendix I
Report on Audit of Customs Forfeiture Fund

Peat Marwick

United States Customs Service
Washington, D.C.

For the purpose of this report, we have classified the significant internal control structure policies and procedures in the following categories:

- General accounting and financial reporting
- Forfeiture of currency
- Forfeiture and sale of property
- General expenditures
- Payments in lieu of forfeiture and reimbursed storage costs
- Revenues from and distributions of assets shared or transferred

For all of the internal control structure categories listed above, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants and OMB Bulletin 91-14. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to ensure that obligations and costs are in compliance with applicable laws; funds, property and other assets are safeguarded against loss, unauthorized use, or misappropriation; and revenues and expenditures applicable to agency operations are properly recorded to permit the preparation of financial statements in accordance with accounting principles described in Note 1 to the financial statements. The condition that we consider to be a reportable condition is included in Exhibit 2 of this report.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. Those conditions that we consider to be material weaknesses are included in Exhibit 1 of this report.

We also noted other matters involving the internal control structure and its operation that we will report to the management of the Fund in a separate letter dated December 31, 1991.

Appendix I
Report on Audit of Customs Forfeiture Fund

 Peat Marwick

United States Customs Service
Washington, D.C.

This report is intended for the information of the Congress, the U.S. General Accounting Office, the management of the Fund and the U.S. Customs Service. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

KPMG Peat Marwick

December 31, 1991

Appendix I
Report on Audit of Customs Forfeiture Fund

Exhibit 1

Customs Forfeiture Fund

Material Weaknesses

ACCOUNTING RECORDS ARE MAINTAINED ON A CASH BASIS

Title 2 of the United States General Accounting Office's Policy and Procedures Manual for Guidance of Federal Agencies requires Federal agencies to maintain accounts of the agency on the accrual basis. The cash basis of accounting may be followed if the differences between the results of cash and accrual accounting are insignificant. U.S. Customs maintains the Customs Accounting and Management Information System (CAMIS) general ledger system for the Customs Forfeiture Fund (hereinafter referred to as the Fund) on a cash basis. As a result, certain account balances differ significantly between the accrual and cash basis of accounting. Accrual accounting contributes significantly to effective financial control over resources and costs of operations and is essential to the development of adequate cost information. Accrual accounting involves identifying and recording costs and revenues in the period in which the revenue is earned or the cost incurred rather than in the period revenue is collected or the cost disbursed. Therefore, in order to comply with the requirements of Title 2 and improve financial information on which decisions are based, we recommend in the following areas, specified procedures be implemented to properly account for transactions on the accrual basis of accounting throughout the year.

Establishing Year End Account Balances

In preparing the year end financial statements, the Fund's management developed manual procedures (e.g. procedures to supplement information contained in the numerous cash basis sub-systems) to identify amounts which should be accrued at year end. These supplemental procedures were necessary because there was not sufficient time after the receipt of the report on internal controls for the 1990 audit to implement the longer term solutions suggested to develop accrual information. As a result of the procedures applied, significant improvement was made over the previous year in capturing year end accrual information. We applaud the effort. However, there were still significant adjustments required in order for the financial statements to be fairly presented. The omissions resulted from:

- Districts not understanding year end accounting instructions;
- Establishing an accounting closing date too soon after year end; and
- Accounting closing procedures did not include all steps necessary to completely capture the needed accrual information.

If such manual procedures are necessary in the preparation of the 1992 financial statements, we recommend management review the procedures and processes to ensure the financial statements presented for audit are more complete. Management's recent decision to defer most system changes for implementation with the AIMS project makes the improvement of the manual supplemental procedures imperative. The review should focus on:

- The completeness and clarity of the instructions;

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- Timing of the accounting closing dates contained in the procedures; and
- Completeness of the procedures performed.

In looking forward, when most of the recommendations that follow are implemented, many of the manual supplemental procedures will no longer be necessary.

Accounts Payable and Accrued Liabilities

Under accrual accounting, a liability is recognized and an expense is incurred when the underlying goods are received or the services have been performed. The Fund generally incurs two types of expenditures. The first type is one for which a physical receipt of goods or services is made at field locations. This receipt is processed through an entry made in the field to the Automated Receiving Report System (ARRS). The corresponding vendor invoice is received at the National Finance Center (NFC) and entered into ARRS. ARRS compares the information on the receiver, the invoice and the related purchase order and if the information is in agreement, posts a liability to the general ledger. A scheduled payment date is also established for 30 days after the invoice date or receiver date, whichever is later.

The above described procedure does not capture the liability for items which have been received and for which an invoice has not been entered into the system. To properly recognize this liability at each month end, an accrual should be posted to the general ledger for all receivers, regardless of whether or not an invoice has been received. ARRS has the capacity to generate an unmatched receiver listing which could be the source to make the appropriate entry. Additionally, an employee at the NFC could review the ARRS listing in order to follow up on old receipts for which no invoice has been received.

The second type of expenditure is one for which there is no indication of physical receipt entered into ARRS; an invoice is received at the field locations. The field locations are responsible for verifying the information on the invoice and when verified, will "certify" the invoice with a stamp and send it to the NFC for payment. The invoice is not entered into ARRS. Rather, it is directly entered to CAMIS by an NFC technician. The payment date is scheduled by the system as 30 days after the invoice date. The services rendered for which these invoices represent should be accrued as a liability when the services have been performed. At our direction, Fund management extended their procedures to identify unrecorded liabilities and found a significant amount of liabilities pertaining to these invoices that were not accrued properly at year end. Thus it appears there is a lengthy time lag between when the field locations receive the invoices and when the invoices are entered into CAMIS. This time lag can be up to 2 months.

An alternative method to properly control and account for these invoices in the short-term is to require field locations to log all invoices received at their locations. This log should include: vendor name, invoice number, invoice date, invoice amount, a description of the charges with the period in time to which the charges relate, the status of the certification process and the date mailed to the NFC. On a monthly basis, a copy of this log should be sent to the NFC. From this information, the appropriate NFC employees can determine whether the invoice has already been received at the NFC and paid, or whether an accrual for the liability is necessary. The appropriate general ledger entry should be made.

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An alternative which could be developed in time involves making necessary system modifications to the Customs Logistics Automated System (CLAS) and ARRS. Currently, contract information is in CLAS for invoices which are received at the field for certification. ARRS could be modified to accept these types of invoices for input, read the CLAS extract file for the related contract information and to differentiate between invoices for accepted or non-accepted goods and services. The invoices then could be received at the NFC and the field personnel could input acceptance directly to ARRS when the goods or services are received. The acceptance by the field would automatically post a journal entry to the general ledger.

ARRS could provide monthly listings of both accepted and non-accepted invoices and provide information for contracts which are still open. The list of accepted invoices provides support for the accounts payable balance on the general ledger. The lists of non-accepted invoices and the open contract information are similar to the unmatched receiver listing ARRS presently has the capacity to generate. These listings could be reviewed by appropriate NFC personnel on a monthly basis to determine a complete liability for services which have been rendered, but for which no bill has been received. An appropriate accrual entry can be recorded in the general ledger based on this information.

In conjunction with these system changes, it would be necessary to formalize procedures for field personnel, including providing them with necessary training. These system modifications, along with the training of and formalized procedures for field personnel, would provide a complete subsidiary ledger to support the general ledger accounts payable balance.

Mortgages and Claims Payable

When the U.S. Customs seizes property, a claim or mortgage may be outstanding against the property. If, upon forfeiture, the property is later sold, the Fund honors the claim or mortgage to the extent of the net proceeds received from the sale of the property or the fair market value if the asset is a vessel or real estate. On the day before payment, the liability is recorded in the general ledger. This is essentially the cash basis of accounting. We recommend the liability be recorded at the time the asset is forfeited. Because this liability reduces the net amount of revenue which will ultimately be realized through the sale of the asset, deferred revenue should be reduced at the time of forfeiture for the amount of the claim against the property.

The seizing officer is responsible for identifying information related to the mortgage or claim at the time the asset is seized. The seizing officer identifies the mortgage or claim through inquiry of the violator. In addition, a public notice is issued through newspapers indicating the property has been seized and any lienholders should notify Customs of any outstanding claims or mortgages.

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Field personnel are now inputting mortgage and claim information into the Customs Property Tracking System (CPTS) as this information is identified. However, a listing of forfeited property with unpaid claims is generated only at year end in order to record the related lien payable and reduce deferred revenue on the general ledger. This information should pass to CAMIS via a journal entry when the related asset is forfeited.

An alternative method to capture all mortgage and claim liabilities in the short-term is to instruct the seizing officer to list all mortgage and claim information as it is identified through the aforementioned procedures. This log should include all relevant information pertaining to the mortgage or claim, such as the lienholder's name, seizure number, description of asset and amount of claim. On a monthly basis, a copy of this log should be sent to the NFC. Appropriate personnel at the NFC could identify the claims which have been paid to date and, for remaining claims, record a liability as previously discussed.

In addition to the aforementioned procedures, it is appropriate for Customs to develop an historical analysis of unidentified mortgages and claims. Because the procedures currently in place to identify such liabilities would not necessarily reveal all mortgages and claims, a liability should be estimated for the amount of yet-to-be identified claims. This estimate should consider historical percentages of claims paid to claims identified by the seizing officer's procedures and should be updated periodically. In this manner, a more complete liability can be recognized in the general ledger and the financial position of the Fund can be more accurately presented.

Forfeited Currency

When U.S. Customs seizes currency, it is retained in a secured area such as sealed evidence bags in a vault at the district house or in a bank safe deposit box. When the currency is declared to be non-evidentiary, the currency is deposited to a U.S. Treasury general bank account and recorded in a suspense account in another Customs fund. Subsequently, the currency is either administratively or judicially declared to be forfeited. Administrative forfeiture occurs when Customs uses their authority, in given circumstances, to declare the currency forfeited. Judicial forfeiture requires the court system to legally decide whether the currency is to be forfeited. Upon forfeiture, the cash becomes property of the Fund and revenue should be recognized. During our audit procedures, we noted a significant time lag between when the districts are notified of the forfeiture and when the NFC is notified of the forfeiture so that revenue can be recorded in the general ledger. This situation arises because the districts hold the forfeiture documentation until all documentation related to the case has been finalized. In some cases, when asset sharing is involved, this process could take longer than a year.

We recommend forfeited currency be recognized as revenue at the time of forfeiture. In the short-term, an alternative method to accomplish this recommendation is to require, at each month-end, each District Fines, Penalties and Forfeiture (FP&F) officer to submit a signed letter to the appropriate individual at the NFC indicating all seizure numbers which were forfeited during the current month. A journal entry could be recorded in the general ledger to recognize the forfeited currency as revenue.

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The Seized Currency Tracking System (SCTS) is designed to account for seized currency from the point of seizure until the seized currency is either returned to the violator or forfeited. The F-13 report, produced from the SCTS, includes information for all currency seizures currently maintained in security vaults, bank suspense accounts, and safe deposit boxes at Customs locations and banks throughout the country.

A possible solution which may be implemented over time is to formalize procedures by which SCTS is updated. Such procedures should include formal training of district employees in the proper use of SCTS and development of written policies to provide guidance. In the future, when the integrity of the data in SCTS is improved, a systems interface between SCTS and CAMIS would automatically update forfeited currency receivable and revenue on the general ledger when a change in status from seized to forfeited is input to SCTS. In addition, SCTS would provide supporting detail for the revenue balance on the general ledger.

Distributions Payable

The Fund, under certain laws and regulations, has the authority to share forfeited property and currency with Federal, state and local agencies who participate either directly or indirectly in a related seizure. In addition, the Fund may transfer forfeited property to other Federal agencies with appropriate approval. Currently, currency shared with state or local agencies is not recognized as a distribution until the cash is disbursed to the other agency. Property shared with or transferred to another agency is not recorded on the general ledger.

A record of approved asset sharing and property transfer transactions is maintained at the Enforcement Assistant Commissioner's office. All asset sharing and property transfer requests, whether approved by Regional or Assistant Commissioners or by the Commissioner, are sent to the Enforcement Assistant Commissioner's office. A possible solution to properly record asset sharing and property transfer transactions is for NFC to access the data base at each month end, and from that information, the proper accrual entry be made. Currently this procedure is only being performed at year end. Because there is sometimes a time lag between when the Regional Commissioner approves an asset sharing and property transfer transaction and when it is received at the Assistant Commissioner's office, a formal procedures directive should be written to instruct the Regional Commissioners to notify headquarters in writing (or other acceptable medium) by month end of all asset sharing and property transfer transactions they have approved for the month. In this manner, the record can be updated and complete for monthly posting of transactions.

Finally, the Seized Property Management System (SPMS) has disposition codes for all seized property held at the contractor. There are disposition codes for property transferred to other Federal agencies and for property shared with state or local agencies. We recommend the balances in these codes be reconciled to the approval records and thus to the general ledger on a monthly basis.

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Accounts Receivable from Contractor

Customs has a contract with EG&G Dynatrend (EG&G) whereby EG&G stores property seized by Customs, conducts auction sales of forfeited property and collects storage costs reimbursed by violators. These cash collections made by EG&G on behalf of Customs are deposited to various bank accounts in the name of EG&G and after approximately one week, are accumulated and deposited to the U.S. Treasury account at the Federal Reserve Bank of New York. Customs receives a validated deposit slip approximately one week later, at which time revenue is recognized.

Under accrual accounting, a receivable should be recorded at the time the revenue is earned (i.e., when the reimbursement from the violator is assessed and when the auction sale is completed.) An alternative method to properly recognize the receivable and revenue is to establish the following formalized procedures. On a monthly basis, EG&G should be instructed to send to the NFC certain information regarding auction sales conducted during the month. (Currently, EG&G sends a "flash report" with limited information.) The information sent should, at a minimum, include the cash received in the auction and the seizure numbers of the assets sold. The NFC can manually record a receivable from the auction sale, along with the related revenue. When SPMS is later integrated with the CAMIS general ledger, the receivable can be updated automatically as the contractor enters sale information to the SPMS system. In addition, the NFC could make the appropriate entries to inventory and mortgages and claims payable by identifying the fair market value of the items sold from SPMS and by identifying associated claims on CPTS.

In connection with the above information EG&G should provide the NFC, EG&G should also provide copies of their statements from the banks to which they deposit Custom's funds. Because, at month end, Customs-owned cash will be in these accounts, EG&G should provide a breakdown of the cash balances (i.e., related to auction sales, reimbursed storage costs). From this information, the Fund can properly recognize a receivable from EG&G and revenue in the general ledger.

When it is determined that property may be returned to the violator, the District FP&F officer completes a disposition order. A copy of the disposition order is sent to EG&G. When EG&G receives the order, EG&G calculates the amount of holding costs owed by the violator and documents this amount on the disposition order. The District Seized Property Custodian should be instructed to update CPTS as to the proper status of seized property. In addition, SPMS has the capacity to track holding costs to be reimbursed by the violator. Thus, EG&G should be instructed to update SPMS when the reimbursement amount is determined. At each month end, an employee at the NFC should compare the seizures to be returned per the CPTS system with the related reimbursements to be received from the SPMS system and the collection deposit slips received from the Federal Reserve Bank of New York to obtain a complete receivable listing from which an accrual can be posted in the general ledger.

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On a monthly basis, an NFC employee should also review the receivables balance to determine the age of individual items which comprise the receivables. Follow-up procedures should be made to determine the status of the receivables. With this process, appropriate adjustments and/or reserves can be determined.

Distribution Payable to U.S. Treasury

The Fund, by law, must remit unobligated amounts in excess of \$15 million to the U.S. Treasury General Fund at the end of the fiscal year. This liability is not recorded on the general ledger of the Fund. It is recognized as a distribution when the transfer takes place. We recommend, on a monthly basis, the calculation of the liability be adjusted and recorded appropriately as a liability on the general ledger.

GENERAL LEDGER

The CAMIS general ledger system processes, groups, and summarizes transactions into account balances for all U.S. Customs funds, including the Forfeiture Fund. CAMIS currently is not utilized to track all balances and transactions that comprise the Fund, such as inventory and revenue, which are tracked by separate systems not directly interfaced with CAMIS. Therefore, complete financial statements cannot be compiled at month end or year end by using the balances contained in the CAMIS general ledger. Rather, information is identified and captured manually from other systems in order to properly compile financial statements. Proper tracking of all information pertaining to the Fund is critical to proper monitoring and analysis of Fund activity. In addition, by not maintaining a complete general ledger for the Fund, it increases the likelihood of not capturing all transactions related to the Fund.

We understand the Asset Information Management System (AIMS) project to revamp the general ledger system is still underway and as a result, management has decided not to make revisions to CAMIS. We have been informed the successful completion of the project may correct the situation noted above. While we understand the decision to not make changes to CAMIS until the AIMS project is complete and be able to produce a complete general ledger for the Fund, we recommend developing a separate trial balance to track all Fund related activity for the production of monthly financial statements to maintain control and an understanding of the Fund's operational results. When the AIMS project is complete, the trial balance can be compared to the financial statements produced from the enhanced general ledger system in order to verify its accuracy.

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FORFEITED INVENTORY

The Fund currently does not record the value of forfeited inventory, and the related deferred revenue, in the general ledger. We recommend forfeited inventory and the related deferred revenue be recorded in the Fund's general ledger at the time of forfeiture. An alternative method to accomplish this recommendation in the short term is to require, at each month-end, each District FP&F officer to submit a signed letter to the revenue branch chief at the NFC indicating all seizure numbers which were forfeited during the current month. (This is same procedure as described under "Forfeited Currency" and the two letters may be submitted in the same reporting package.) A journal entry should be recorded to the general ledger to recognize the forfeited inventory asset and the related deferred revenue. An appropriate individual at the NFC should compare this information to the inventory subsidiary systems (SPMS and CPTS) and investigate differences.

During our audit procedures, we noted inventory listings produced by SPMS and CPTS contained inaccurate data about inventory on hand. We identified items at the physical inventory observation locations that were not listed on the SPMS reports and also items that remained on the SPMS reports that had already been sold, transferred, or disposed. One cause of these problems is that documentation for seizures is not prepared and input to SPMS and CPTS on a consistent and timely basis.

Also during our audit procedures, we noted the final inventory listings produced by CPTS failed to include all forfeitures occurring in the current fiscal year. The main cause of this problem is the FP&F staff are not properly monitoring and updating their systems to reflect the change in inventory status and are not communicating the change in status to the appropriate personnel to update CPTS and/or SPMS.

A possible solution which can be implemented is to formalize procedures by which FP&F staff are required at the end of each day to forward the disposition order for new forfeiture information to the appropriate personnel to update CPTS and/or to EG&G to update SPMS to reflect changes in inventory status. Additionally, FP&F staff would be required to specifically identify and report to the NFC the status of all seized inventory items older than six months or with appraised/fair market values greater than \$50,000. Formalized procedures by which CPTS and SPMS are updated and maintained should be developed and maintained. Such procedures should include formal training of FP&F and district employees as well as written policies providing guidance to FP&F, district, and EG&G employees. Lastly, a systems interface between CAMIS or AIMS and CPTS or SPMS should be developed to record changes in status on CPTS or SPMS from seized to forfeited on the general ledger inventory balance.

FORFEITED INVENTORY VALUATION

Under the 1930 Tariff Act and later amendments, Customs enforces importing and exporting and drug-related laws of the United States. Accordingly, when violations are discovered, Customs has the authority to seize the possessions of the violator at the time of seizure. The seized property may eventually be returned to the violator upon payment of a penalty or if the violation is cured or otherwise dismissed. However, if the possessions are not returned to the violator, the property is forfeited to Customs through either administrative or judicial procedures. Once forfeited, the property is either retained for official use of Customs, destroyed, sold, or transferred to another state, local, or federal agency.

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Generally, for financial reporting purposes, inventory should be stated at the lower of cost or market. However, it is not reasonably possible to determine approximate costs related to the seizure of forfeited property. Therefore, inventory of forfeited property should be valued at its net realizable value to Customs. Because it is Custom's intention to sell some of the forfeited property at auction, net realizable value--in these circumstances--should be the expected estimated selling price of the forfeited property. Further, because it is not reasonably possible to determine the approximate costs of forfeited property, the estimated selling price of forfeited property sold at auction should be the basis for determining the net realizable value of forfeited property which is retained by Customs, shared with state and local agencies, or transferred to other federal agencies.

Inventory value of forfeited property is currently recorded in SPMS at appraised value, determined at seizure by the seizing agent, import specialist, or at its fair market value, determined by independent appraisal immediately before its sale at auction. While this information is important to report the value of seizures to Congress and to the American public, it should not be used in all instances for financial reporting purposes. Forfeited property, such as counterfeit goods, controlled substances, and other seizures which must ultimately be destroyed, should reflect a net realizable value of zero for financial reporting purposes.

Using seizure values, in particular, for financial reporting purposes is misleading because inventory is overvalued and does not present an accurate picture of the net realizable value to Customs for forfeited property. For example, a seizure of illegal drugs was recorded in SPMS at its street value of approximately \$700,000. However, because these drugs will ultimately be destroyed, the net realizable value to Customs is actually zero. Therefore, for financial reporting purposes, we recommend Customs assign a zero value to forfeited property that will ultimately be destroyed. In addition, we recommend Customs evaluate the accuracy of market values assigned to forfeited property in SPMS. This could be achieved by comparing these values to the actual sales proceeds obtained at subsequent auction sales.

For the 1991 financial statements, management developed a historical analysis of the ultimate sales values compared to the initial appraised amounts. This ratio is applied to the ending inventory amount to value inventory at its anticipated net realizable value. This analysis is an important first step to properly value inventory. We encourage management to continue reviewing this analysis to refine its accuracy and ease in preparation. As the process is refined, it will become easier to prepare the analysis monthly to properly reflect month end inventory balances.

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Exhibit 2

Customs Forfeiture Fund

Reportable Condition

UNLIQUIDATED OBLIGATIONS

The Fund records all commitments in the unliquidated obligations account. Throughout the year when invoices are received for actual purchases, the balance in the account is reduced. In our audit procedures, we found a significant amount of obligations that appear to be dormant or that need to be written-off.

Two procedures exist that enable an obligation to be written-off. First, when an invoice is sent to the NFC for payment and marked as "final payment," this is the indication to the NFC that any remaining obligation should be eliminated. Second, when an official requesting the obligation sends notice to the NFC to write-off the obligation as it is no longer necessary. In our audit procedures, we noted these procedures are not being followed.

We recommend additional procedures be implemented during the quarterly review of the outstanding unliquidated obligations. Currently, a summary report of all obligations are sent to the Customs Budget Official, who is to review the report to determine the validity of the obligations. However, due to the amount of dormant unliquidated obligations currently in the account, it appears this procedure has not been effective. We recommend a report be generated containing all obligations outstanding greater than one year. The report should be sent directly to the official originating the obligations notifying him that unless the field notifies the NFC within a stated number of days, the obligation will be written-off. Although this process is effective for eliminating dormant obligations, management should contact legal council prior to implementing the recommendation to determine its legality.

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Supplemental Financial and Management Information

UNITED STATES CUSTOMS SERVICE
Asset Sharing Summarized by State and U.S. Territories
Fiscal Year 1991
(Dollars in thousands)
(Unaudited)

State	Currency Value	Property Value
Alabama	\$ 407	254
Alaska	24	-
Arizona	1,293	508
California	50,942	1,125
Colorado	-	88
Florida	11,413	578
Georgia	13	80
Guam	19	-
Hawaii	789	-
Idaho	40	-
Illinois	55	-
Iowa	-	3
Kentucky	-	50
Louisiana	78	1
Maine	28	-
Maryland	35	55
Massachusetts	30	-
Michigan	1,034	-
Minnesota	54	-
Mississippi	845	170
Missouri	116	-
Montana	189	-
Nevada	73	-
New Jersey	43	-
New Mexico	206	160
New York	15,361	107
North Carolina	88	4
North Dakota	35	-
Ohio	45	12
Oklahoma	47	636
Oregon	409	9
Pennsylvania	240	4
Puerto Rico	-	12
Tennessee	80	-
Texas	15,047	405
Utah	6	18
Vermont	-	1
Virginia	32	-
Washington	123	-
Total	\$ 99,239	4,280

Summarized above are the currency and property values of assets forfeited and shared with state and local agencies and U.S. territories participating in the seizure. This supplemental schedule is not a required part of the basic financial statements of the Customs Forfeiture Fund. Information in this schedule does not agree with total assets shared with state and local agencies in the financial statements of \$95,205 as it includes some distributions relating to fiscal year 1990 and it does not include the adjustment to present property distributed at net realizable value.

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Supplemental Financial and Management Information

**CUSTOMS FORFEITURE FUND
UNITED STATES CUSTOMS SERVICE**

Uncontested Seizures of Monetary Instruments Valued Over \$100,000,
Taking More than 120 Days From Seizure to Deposit in Forfeiture Fund

Fiscal Year 1991

(Dollars in thousands)

(Unaudited)

<u>Region/Districts</u>	<u>Uncontested Total Dollar Values</u>	<u>Total Number of Cases</u>
Northeast	\$ -	-
Region totals	-	-
New York		
New York Seaport	12,262	24
Newark	569	2
JFK	<u>16,890</u>	<u>37</u>
Region totals	29,721	63
North Central		
Chicago	<u>665</u>	<u>2</u>
Region totals	665	2
Southeast		
Tampa	342	1
San Juan	405	2
Miami	<u>20,440</u>	<u>34</u>
Region totals	21,187	37
South Central		
Mobile	<u>675</u>	<u>1</u>
Region totals	675	1
Southwest		
Laredo	3,646	6
El Paso	1,300	3
Houston	<u>12,978</u>	<u>29</u>
Region totals	17,924	38
Pacific		
San Diego	385	3
Los Angeles	14,114	28
Seattle	<u>205</u>	<u>1</u>
Region totals	14,704	32
National totals	\$ 84,876	173

19 USC 1607 (c), as amended (Public Law 101-382) requires Customs to report annually to Congress uncontested seizures of monetary instruments or proceeds over \$100,000, which were not deposited in the Customs Forfeiture Fund within 120 days of the seizure date.



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