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SUBCOMMITTEE ON THE DEPARTMENTS OF TRANSPORTATION AND TREASURY, AND INDEPENDENT AGENCIES

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Chairman Istook, Ranking Member Olver, members of the Subcommittee and Subcommittee staff – Good morning.

I appreciate the opportunity to testify about the management challenges currently facing the Department of Treasury including the OIG and how they have been impacted by the divestiture pursuant to the Homeland Security Act of 2002.

I am also pleased to be here with Acting Treasury Inspector General for Tax Administration (TIGTA) Pamela Gardiner. As you know, the President's fiscal year 2004 budget has proposed a consolidation of our office and TIGTA into a new Inspector General office to be called the Inspector General for Treasury.

Before I begin discussing what things look like at present and what they will look like going forward, I want to make one brief comment on the past.

This organization, since it became a statutory OIG, has seen a great deal of change. In his March 2001 testimony before the Subcommittee, our Inspector General discussed the period of turmoil that had occurred as certain Treasury Office of Inspector General (OIG) officials were then the subject of investigations and the fact that between February 1998 and July

1999, the workforce had been led by three Senate-confirmed IGs and an Acting IG. I was the Assistant Inspector General for Audit during that period and I can attest to the fact that it was a very difficult time. I am proud of the fact that we stayed focused on our core mission throughout that period of turmoil and in fact grew stronger and better under the leadership of our current Inspector General. Having said that, the divestiture of nearly 70 percent of our workforce to the new Department of Homeland Security presents perhaps the greatest challenge to date in meeting our mission. Through all of this I am still confident that going forward the career management and staff of the Treasury OIG will continue to stay focused on our core mission of conducting audits and investigations. The Treasury Department still has a great deal of important work to do and we still have a lot of important oversight to do.

I would like to briefly describe some of the important work of the Department that we are responsible for auditing and investigating, post-divestiture. I will then discuss our organization post divestiture and our capabilities to continue to conduct audits and investigations of those remaining Treasury operations. Finally, I will discuss my perspective on the significant issues facing the Department of the Treasury.

As you know, the Treasury Department divested almost all of its law enforcement activities by transferring the U.S. Customs Service, the U.S. Secret Service, and the Federal Law Enforcement Training Center to the Department of Homeland Security and transferring the non-revenue functions of the Bureau of Alcohol, Tobacco and Firearms (ATF) to the Department of Justice. The collection of about $22 billion annually in revenue was also transferred to the Department of Homeland Security with the transfer of Customs. While these functions represent a significant part of the non-IRS Treasury mission, there are still eight non-IRS Treasury bureaus and significant programs and functions in the Department that remain behind.

Our universe of work covers approximately 16,000 Treasury employees who provide a wide range of services throughout the United States and in many foreign countries.

Following is a summary of the diverse and complex non-IRS bureaus, programs, and activities that comprise the Department of the Treasury post-divestiture.

Departmental Offices (DO)

DO's function in the Department of the Treasury is to provide basic support to the Secretary. The Secretary maintains the primary role in formulating and managing the domestic and international tax and financial policies of the Federal government. In support of the Secretary, resources are provided for policy formulation and implementation in the areas of domestic and international finance, investment, tax, trade, financial operations, and general fiscal policy. Resources are also provided for administrative support to the Secretary and policy components, and coordination of Departmental administrative policies in financial and personnel management, procurement operations, and automated information systems and telecommunications.

What can sometimes be overlooked when viewing the Department is that it is not just an organization of high level officials setting policy and providing broad oversight to the Treasury bureaus. The Department has numerous operations and activities with their own specific operational missions. These operations and activities manage and/or disburse hundreds of millions and in some cases, billions of dollars. Some of those that should be noted include:

- The **Office of Foreign Assets Control (OFAC)** manages and enforces economic sanctions and embargo programs against targeted foreign governments and groups that pose threats to the national security, foreign policy, or economy of the United States. These include sanctions programs administered under the International Emergency Economic Powers Act, the Trading with the Enemy Act, the United Nations Participation Act, the Anti-Terrorism and Effective Death Penalty Act, the Foreign Narcotics Kingpin Designation Act, and other related Executive Orders and statutes. Since September 2001, OFAC and our allies have blocked terrorist-related assets totaling $124 million worldwide. OFAC currently administers 23 economic sanctions programs involving blocked targets, trade embargoes, or other restrictions. These sanction programs include terrorists, terrorist governments and organizations, international narcotics traffickers, hostile governments and others. OFAC is also authorized to block the domestic financial transactions of prohibited governments, organizations and individuals. During 2002, OFAC had frozen as much as $36 million in domestic accounts associated with terrorist financing.

- Recently, the Department announced the creation of a new **Executive Office for Terrorist Financing and Financial Crimes (EOTF/FC)** reporting to the Deputy Secretary. This office has been charged with coordinating and leading the Department's multi-faceted efforts to combat terrorist financing and other financial crimes, both within the United States as well as abroad.

  EOTF/FC will work closely with other offices within Treasury and throughout the Federal government to identify, block, and dismantle sources of financial support for terror and other criminal activities, including money laundering. In addition, the team will work with international partners to expand the fight against terrorist financing and financial crimes in other nations. The office will focus on reducing the risk that domestic and international financial systems are being misused by criminals and terrorists.

  EOTF/FC is charged with the following duties: developing and implementing Federal government strategies to combat terrorist financing domestically and internationally (in concert with Treasury's International Affairs Task Force on Terrorist Financing); developing and implementing the National Money Laundering Strategy, as well as other policies and programs to fight financial crimes; participating in the Department's development and implementation of Federal government policies and regulations in support of the USA PATRIOT Act, including outreach to the private sector; joining in representation of the United States at focused international bodies dedicated to fighting terrorist financing and financial crimes; and developing Federal government policies relating to financial crimes.

  EOTF/FC will provide policy guidance for the Financial Crimes Enforcement Network as it works with the financial sector, the law enforcement community, and foreign financial intelligence units to foster cooperation against domestic and international financial crimes. Also, the office will provide policy guidance to OFAC.

- DO's **Office of D.C. Pensions** was established to implement the Balanced Budget of 1997, as amended, and to make timely and accurate Federal benefit payments associated with the District of Columbia Retirement Programs for police officers, firefighters, teachers, and judges. In fiscal year 2002, Federal benefits were paid to approximately 13,300 retirees and survivors. Federal benefit and refunded employee contribution payments are expected to be approximately $470-$540 million per year for the next 7 years. As of September 30, 2002, assets for funding the retirement programs were $4 billion and liabilities were $8.4 billion, resulting in an unfunded pension liability of $4.4 billion.

- The **Air Transportation Stabilization Board (ATSB)** was created by Public Law 107-42 to issue Federal credit instruments (loan guarantees) to assist air carriers that suffered losses as a result of the terrorist attacks on the United States that occurred on September 11, 2001. The ATSB reviews and makes decisions on loan guarantee applications, and is authorized to issue up to $10 billion in loan guarantees. The ATSB made one loan guarantee in fiscal year 2002 to guarantee approximately $380 million of a $429 million loan from a commercial lender to an air carrier. As reported by the Department, the ATSB, as of November 7, 2002, had four applications conditionally approved representing approximately $1.3 billion in gross loans and $1.2 billion in loan guarantees. Additionally, another seven applications, representing approximately $2.3 billion in gross loans and $2.1 billion in loan guarantees, were pending approval and were being processed. It should be noted, however, that loan terms and guaranteed amounts are subject to significant fluctuation until the closing date.

- The Secretary of the Treasury through the **Exchange Stabilization Fund (ESF)** is authorized to deal in gold and foreign exchange and other instruments of credit and securities as deemed necessary, consistent with U.S. obligations in the International Monetary Fund, regarding orderly exchange arrangements and a stable system of exchange rates. The principal source of the fund's income is earnings on investments held by the fund, including interest earned on fund holdings of U.S. Government securities. The fiscal year 2004 estimated net position of the fund is $30.8 billion.

- The **Community Development Financial Institutions (CDFI) Fund** provides equity investments, grants, loans, and technical assistance to new and existing community development financial institutions. Funds provided by the CDFI Fund are expected to enhance the capacity of these institutions to finance economic development, including small businesses, community facilities, housing, and other community development initiatives in distressed urban, rural, Native American, Native Hawaiian, and Alaska Native communities. The CDFI Fund also provides grants to insured depository institutions to facilitate investment in CDFIs and increase community lending activities. In addition, the CDFI Fund administers the New Markets Tax Credit Program by providing allocations of tax credits to Community Development Entities (CDEs), which in turn provide the tax credits to entities that invest in the CDEs.

For fiscal years 2000 through 2002, the various types of financial and technical assistance provided by the CDFI Fund totaled approximately $298.5 million. As a new program, New Market Tax Credit awards will begin in fiscal year 2003. The fiscal year 2004 estimated net budget authority for the CDFI Fund is $51 million.

- The **Federal Financing Bank (FFB)** was created in 1973 to reduce the costs of Federal and Federally-assisted borrowing and to ensure the coordination of such borrowing from the public in a manner least disruptive to private financial markets and institutions. FFB loans are now used primarily to finance direct agency activities such as construction of Federal buildings by the General Services Administration and meeting the financing requirements of the U.S. Postal Service. In certain cases, the FFB finances Federal direct loans to the public that would otherwise be made by private lenders and fully guaranteed by a Federal agency. The estimated FFB loans outstanding balance at the end of fiscal year 2004 is $30.4 billion.

A number of other accounts and activities are managed by DO. Examples include: (1) a working capital fund; (2) the Sallie Mae Fund to provide for enhanced financial safety and soundness oversight of the Student Loan Marketing Association by the Department; (3) an account to provide for technical assistance to other countries in support of the Department's responsibility to formulate, conduct, and coordinate the international financial policies of the United States; and (4) accounts related to the United States' participation in the International Monetary Fund and multilateral development banks. This list is by no means exhaustive, but is indicative of the variety and complexity of activities that are the responsibility of the Department.

Alcohol and Tobacco Tax and Trade Bureau (TTB)

The newly created TTB will, as ATF did before it, administer and enforce the existing Federal laws and tax code provisions related to the production and taxation of alcohol and tobacco products. This amounts to approximately $15 billion in excise taxes, including $100 million in occupational tax on the manufacture of firearms and ammunition.

In practical terms, it is anticipated that alcohol producers and wholesalers, as well as tobacco manufacturers, importers, and exporters, will see little or no change beyond the name of the agency. TTB will continue collecting Federal alcohol and tobacco excise taxes and classifying alcohol and tobacco products for excise tax purposes. TTB will also investigate applications and issue permits for the operation of distilleries, wineries, and breweries, and for tobacco manufacturers, importers, and exporters. In addition, the bureau will continue Federal regulatory oversight of the operations of various industrial users of distilled spirits, including manufacturers of non-beverage products, tax-free, and denatured alcohols.

Protecting the consumer remains a major function under TTB through the regulation of the production, packaging, bottling, labeling, and storage of alcohol and tobacco products. TTB will ensure that alcohol beverage labeling and advertising provides adequate information to consumers concerning the identity and quality of the products. TTB is also responsible to ensure fair trade practices by regulating the marketing and promotional practices of alcohol beverage producers and wholesalers. As was the case under ATF, this is done primarily through the investigation of allegations of illegal trade practices.

Bureau of Engraving and Printing (BEP)

BEP manufactures the financial and other securities of the United States. Accordingly, the Bureau designs, prints, and furnishes a large variety of security products, including Federal Reserve notes, U.S. postage stamps, Treasury securities, identification cards, naturalization certificates, and other special security documents. All products are designed and manufactured with advanced counterfeit deterrence features to ensure product integrity, and the Bureau advises other Federal agencies on document security matters.

The Bureau also processes claims for the redemption of mutilated currency. The Bureau's research and development efforts focus on the continued use of automation in the production process and counterfeit deterrent technologies for use in security documents, especially U.S. currency. For fiscal year 2004, BEP estimates 8.5 billion in currency deliveries and 7.5 billion in postal and revenue stamp requirements.

BEP is in the process of redesigning our nation's currency. The new design, known as NexGen, will affect the $100, $50, and $20 notes. Introduction of the NexGen $20 bill will begin as early as the fall 2003, with introduction of the other notes 12 to 18 months later. The NexGen design will build on past security features with the addition of subtle background colors and other new security features that are designed to deter counterfeiting. An extensive public education campaign is planned to inform the public and business sector about the NexGen currency and also how to detect counterfeit currency.

BEP operations are currently financed by means of a revolving fund. The underlying legislation requires BEP to be reimbursed by customer agencies for all costs of manufacturing products and services performed. Bureau operations during 2002 resulted in a decrease to retained earnings of $29 million.

Financial Management Service (FMS)

FMS has four major activities: payments, collections, debt collections, and government-wide accounting and reporting.

FMS implements payment policy and procedures for the Federal government, issues and distributes payments, promotes the use of electronics in the payment process, and assists agencies in converting payments from paper checks to electronic funds transfer (EFT). The control and financial integrity of the Federal payments and collections process includes reconciliation, accounting, and claims activities. The claims activity settles claims against the United States resulting from Government checks which have been forged, lost, stolen, or destroyed, and collects monies from those parties liable for fraudulent or otherwise improper negotiation of Government checks. Each year FMS issues 950 million non-Defense payments, with a dollar value of more than $1.2 trillion, to a wide variety of recipients, such as those who receive Social Security, IRS tax refunds, and veterans' benefits. FMS estimates that for fiscal year 2004, it will make 238 million check payments and 696 million electronic payments, and receive 1.4 million claims.

FMS implements collections policy, regulations, standards, and procedures for the Federal government, facilitates collections, promotes the use of electronics in the collections process, and assists agencies in converting collections from paper to electronic media. Over $2 trillion is collected annually through both electronic and paper-based mechanisms.

Pursuant to the Debt Collection Improvement Act of 1996, FMS provides debt collection services to client agencies which includes collection of delinquent accounts, offset of Federal payments against debts owed the Government, post-judgment enforcement, consolidation of information reported to credit bureaus, reporting for discharged debts or vendor payments, and disposition of foreclosed property. FMS estimates that during fiscal year 2004 it will collect $2.9 billion in delinquent debt using all available tools.

FMS provides financial accounting, reporting, and financing services to the Federal government and the Government's agents who participate in the payments and collections process by generating a series of daily, monthly, quarterly and annual Government-wide reports. FMS also works directly with agencies to help reconcile reporting differences.

FMS also manages a number of other accounts on behalf of the Federal government. These accounts include, for example: (1) Payment to the Resolution Funding Corporation to cover interest payments on obligations issued by the Resolution Funding Corporation ($1.7 billion in fiscal year 2004 estimated net budget authority); (2) Interest Paid to Credit Financing Accounts ($3.8 billion in fiscal year 2004 estimated net budget authority); and (3) Claims, Judgments, and Relief Acts ($935 million in fiscal year 2004 estimated net budget authority).

Financial Crimes Enforement Network (FinCEN)

FinCEN, created in 1990 and elevated to bureau status in 2001, supports law enforcement investigations to prevent and detect money laundering, terrorist financing, and other financial crimes. FinCEN links law enforcement, financial, and regulatory communities into a single information-sharing network. Using Bank Secrecy Act (BSA) information reported by banks and other financial institutions, FinCEN serves as the nation's central clearinghouse for broad-based financial intelligence and information sharing on money laundering. This information helps illuminate the financial trail for investigators to follow as they track criminals and their assets.

FinCEN provides BSA guidance to more than 220,000 financial institutions that are subject to its reporting and record keeping requirements. During fiscal year 2002, FinCEN received more than 261,000 individual reports of suspected illegal acts, referred to as Suspicious Activity Reports, and 12.4 million Currency Transaction Reports from these institutions when they receive $10,000 in cash or a monetary equivalent.

Through its investigative analysis efforts, FinCEN provides support for the investigation and prosecution of law enforcement cases at the Federal, state, local and international levels, using financial data collected under the BSA, as well as other commercial and law enforcement information. FinCEN serves as a catalyst for research, analysis, and dissemination of information on money laundering methods and trends through joint case analysis with law enforcement, integration of all source information, and the application of state-of-art data processing techniques. FinCEN also establishes policies to administer the BSA effectively while balancing the associated burden imposed on the regulated financial institutions. Internationally, FinCEN maintains in-depth, country-specific expertise concerning money laundering, terrorist financing, and other financial crimes around the world to assist decision makers in developing and promoting U.S. Government anti-money laundering policies. FinCEN also uses this expertise to promote the development of Financial Intelligence Units in other countries, and to facilitate investigative exchanges with them.

FinCEN's regulatory support program supports new requirements to strengthen anti-money laundering controls with the money services business industry, casino, broker/dealer, securities, and other industries with new program or reporting requirements under the BSA. The USA PATRIOT Act expanded anti-money laundering program and reporting requirements to a number of industries previously not covered by the BSA. FinCEN will undertake programs to reach these new industry groups, as necessary. FinCEN will also continue efforts with the IRS, especially related to the money service business industry, to assure compliance, respond to public inquiries, distribute forms and publications, and support information processing of the BSA data.

U.S. Mint

The Mint manufactures coins, sells numismatic and investment products, and provides for security and asset protection. Public Law 104-52 established the United States Mint Public Enterprise Fund (PEF), a revolving fund that encompasses a number of funds related to the Mint. Among other things, the PEF legislation requires the Mint to submit annual audited business-type financial statements to the Congress and exempts the Mint from provisions of law governing procurement or public contracts.

The Mint's operations are divided into three major activities: Circulating Coinage, Numismatic and Investment Products, and Protection. The Circulating Coinage activity funds the manufacture of circulating coins for sale to the Federal Reserve System as determined by public demand. In 2004, it is anticipated that this activity will manufacture 13.8 million coins. The Mint is credited with receipts from its circulating coinage operation, equal to the full cost of producing and distributing coins that are put into circulation. From that, the Mint pays its cost of operation. The difference between the face value of the coins and these costs are profit, which is deposited as seigniorage to the general fund. In 2002, the Mint transferred $1.03 billion to the general fund. The Numismatic and Investment Products activity funds the manufacture of numismatic and bullion coins, medals, and other products for sale to collectors and the general public. The Protection activity funds protection of the Federal government's stock of gold and silver bullion, coins, Mint employees and others, and Mint property utilizing police officers and modern protective devices.

Bureau of the Public Debt (BPD)

Treasury manages the nation's debt through BPD. BPD oversees the $6.3 trillion Federal debt, including the $3.6 trillion held by the public and $2.7 trillion held by Federal agencies. Last year, BPD issued approximately $3.7 trillion of debt by auctioning marketable Treasury securities and selling savings bonds, and paid off $3.5 trillion in securities. The estimated interest on Treasury securities for fiscal year 2004 is approximately $353 billion.

BPD's responsibilities include: (1) implementing regulations governing the primary issuance of Treasury securities and secondary market transactions involving government securities;

(2) issuing and servicing of Treasury securities; (2) conducting transactions on outstanding securities including exchanges, transfers, and redemptions; (3) receiving, auditing, recording, storing, and destroying redeemed securities and interest coupons; (4) protecting the investor by adjudicating claims on lost, stolen, or destroyed securities; (5) establishing and maintaining accurate records of the sale and redemption of savings bonds; (6) issuing and accounting for investments on behalf of more than 200 Government agencies and Federal Trust Funds; (7) conducting auctions, and announcing auction results in a timely manner; (8) recording and reporting accurate financial data concerning the public debt; and (9) providing quality customer service and convenience to the investor by making savings securities available through a nationwide network of financial institutions, by issuing marketable securities directly and through the Federal Reserve Banks, and by enabling investors to request information and complete financial transactions using emerging electronic technologies. An important goal of BPD is a multiyear effort to convert all savings bond holdings to paperless form.

Office of the Comptroller of the Currency (OCC)

OCC was created for the purpose of establishing and regulating a national banking system. As the administrator of national banks, OCC charters new banking institutions after investigation and due consideration of charter applications. Supervision of existing national banks is aided by the required submission of periodic reports and detailed onsite examination, which are conducted by a staff of approximately 1,900 national bank examiners. At present, there are approximately 2,100 national banks and 52 Federal branches with total assets of more than $3.8 trillion. These assets represent approximately 58 percent of the total assets of all commercial banks. In addition, OCC promulgates rules and regulations for the guidance of national banks and bank directors. The OCC budget is derived principally from assessments paid by national banks and interest on investments in U.S. Government securities.

Office of Thrift Supervision (OTS)

OTS was created by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, assuming the regulatory functions of the Federal Home Loan Bank Board dissolved by the same act. OTS charters, regulates, and examines Federal thrifts that are insured by the Savings Association Insurance Fund (SAIF). In addition, OTS cooperates in the examination and supervision of state-chartered thrifts insured by the SAIF. OTS sets capital standards for Federal and state thrifts and reviews applications of state-chartered thrifts for conversion to Federal thrifts. As of September 30, 2002, OTS oversees 983 thrifts with total assets of $987 billion. Similar to OCC, OTS' income is derived principally from assessments on thrifts, examination fees, and interest on investments in U.S. Government obligations.

ORGANIZATION, STAFFING AND MISSION OF THE OIG

The Treasury OIG was established in 1989 by the Secretary of the Treasury as a result of the 1988 Amendments to the Inspector General Act. The Inspector General of the Department of the Treasury exercises all the duties and responsibilities of an Inspector General for the Department other than those exercised by TIGTA. That office was established as a result of the Internal Revenue Service Restructuring and Reform Act of 1998. The Treasury OIG also oversees, on behalf of the Inspector General community, the operations of the Inspectors General Auditor Training Institute. The Institute is the primary source of training for auditors in the Inspector General community.

For fiscal years 2002 and 2003, our net authorized budget authority was $35,397,000 and $35,504,000, respectively, and our authorized full time equivalent (FTE) positions were 282 for both years. In anticipation of divestiture to the Departments of Homeland Security (DHS) and Justice OIGs, last fall we prepared various analyses of our level of effort devoted to the Treasury bureaus and functions to be divested to DHS and the Department of Justice. We estimated this to be a little over 30 percent in total. Our office was directed to divest 155 positions to the DHS OIG and 40 positions to the Justice OIG. This total divestiture of 195 out of 282 FTE represents nearly 70 percent of our staffing.

Between March 9 and September 30, 2003, we will go through a dramatic reduction in on-board strength, having started this fiscal year with 282 full time positions and ending the fiscal year with 87 full time positions. During this reduction in strength, we need to ensure that there is no breakdown in the oversight of the bureaus being divested or retained by the Department. We are coordinating closely with both the DHS OIG and the Justice OIG to effectively complete the transition of ongoing work. Another challenge that we need to plan for over the next 7 months is the proposed consolidation of our office with TIGTA.

I will now discuss in more detail the impact of divestiture to each of our operating components.

Office of Audit

The Office of Audit's post-divestiture strength has been significantly reduced. Pre-divestiture, we had an extensive field office structure located in eight cities plus a Headquarters staff in Washington, D.C. The authorized FTE level for the Office of Audit was 165. Except for a small field office remaining in San Francisco, our audit operations are now centralized in Washington, D.C. We anticipate an authorized staffing level of 52 FTE, post divestiture. Of note, our Financial Audit division decreased significantly as did our Information Technology (IT) Audit division. Also we will no longer be able to maintain an Evaluations function.

What did not go away with divestiture is our mandated audit work. These mandates include our: (1) audit responsibility for the Department's consolidated financial statements and the financial statements of 11 other component entities, (2) responsibility to conduct an annual independent evaluation of the Department's information security program and practices under the Federal Information Security Management Act of 2002 (FISMA), and (3) responsibility under the Federal Deposit Insurance Act to conduct material loss reviews of failed financial institutions supervised by OCC or OTS that result in significant losses to deposit insurance funds.

Meeting our mandates has always presented a challenge. As we testified in March 2001, Treasury, with responsibility for collecting 98 percent of the revenue, managing the $6.2 trillion dollar debt, and performing the central accounting functions for the Federal Government, is a tall order. With respect to auditing the Department's financial statements, this past year we completed the audit of Treasury's financial statements by November 15, 2002, well ahead of the accelerated deadline of January 31, 2003, established by OMB.

We have worked very hard since the passage of the Chief Financial Officers Act to build and maintain one of the strongest financial statement auditing capabilities in the Federal government. I am proud of the efforts of our financial auditors, our program auditors who were temporarily assigned to these audits, as well as the contractors who performed substantial portions of the audit work under our oversight.

Although our financial audit staff will now be about half of what it was, the work necessary to accomplish the financial statement audits of the Department and remaining entities has not been lessened significantly. Our challenge will be to re-establish the capacity to deliver the excellent financial audit services we have in the past.

Furthermore, over the last 3 years we built up our IT auditing capacity as well. Among other things, this enabled us to meet the requirement to annually evaluate, in a substantive and timely manner, the Department's information security program and practices in accordance with the Government Information Security Reform Act (GISRA). This was a significant effort by our office this year, and we anticipate that it will be more challenging under the expanded requirements of FISMA. Similar to our financial audit staff, our IT audit division is now half its previous size. Nevertheless, the Department still operates over 450 systems, including FMS' huge payment and accounting systems, TTB's revenue systems, and BPD's debt systems, to name a few.

As mentioned above, our Program Audit division has also been significantly impacted by divestiture. The major mandate of this division is to perform material loss reviews (MLR) of failed financial institutions. Since this mandate became effective in 1993, we have performed seven such reviews. However three of them were performed during this past fiscal year with two occurring simultaneously. Our experience has been that these reviews are resource intensive, each requiring 6 to 7 auditors for up to 6 months. While initially this work was primarily performed out of our San Francisco office, we sought to expand our skill set by assigning staff from our other field offices to assist on the last three reviews. These newly trained individuals were transferred to DHS OIG with the divestiture. Despite the heavy demands by MLRs on our resources, we were in the past able to meet this and other requirements identified above while, at the same time, addressing congressional requests for work and auditing significant Departmental vulnerabilities. Looking forward, our office is fully committed to accomplishing our mandated requirements; however, with our current staffing level, we will have to make tough choices about the other work we can undertake.

Office of Investigations

Before divestiture, the Office of Investigations was staffed with investigators and support personnel staff located in

Washington, D.C., and seven field offices nationwide. The authorized staffing level was 72 FTE. Post-divestiture, that staff has been significantly reduced. We anticipate an authorized FTE level of 22 with all positions located in Washington, D.C.

Although a significant volume of work was transferred to DHS OIG and Justice OIG when the law enforcement bureaus left Treasury, the manufacturing bureaus with facilities both inside and outside of Washington, D.C., remain under our investigative oversight. Specifically, the Mint has facilities in Philadelphia, West Point, Ft. Knox, Denver, and San Francisco, and BEP has a facility in Fort Worth, Texas. Investigations at these facilities will now need to be conducted exclusively by our Headquarters-based staff, creating a significant burden on our travel resources. Additionally, OCC and OTS have bank examiners throughout the country who are also subject to our investigative oversight.

As I discussed previously, along with the divestiture of ATF's enforcement activities to Justice, the Homeland Security Act created a new bureau within Treasury responsible for administering alcohol and tobacco tax laws and implementing regulations previously administered by the ATF. This new bureau, TTB, will have approximately 560 employees. Previously, ATF had a substantial internal affairs function and we generally focused our investigative resources on only the most senior management officials. The internal affairs function of ATF transferred to Justice along with the enforcement functions of ATF. The new TTB will not have an internal affairs function, and we will be responsible for all investigations that need to be conducted in TTB. Thus our investigative caseload relative to the old ATF could stay the same or even increase.

Office of Counsel

Divestiture has impacted the Office of Counsel as well. We will be divesting all but two of our attorneys to the DHS OIG. Even so, with a reduced work force, the Office will still be responsible for responding to requests for information and records of the OIG, such as Giglio requests from U.S. Attorneys' offices for information about Treasury employees who are witnesses in criminal trials, as well as Freedom of Information Act requests, and discovery requests in civil and criminal litigation where OIG reports or personnel are relevant. The universe of requests and records will continue to include investigations and audits relating to personnel and activities in bureaus that have been divested. We also expect to retain responsibility for personnel litigation before the Merit Systems Protection Board and the Equal Opportunity Employment Commission involving employees transferred from the OIG. Depending on workload, we may need to obtain legal services from elsewhere to meet all such obligations.

<u>Office of Management</u>

Prior to divestiture, the OIG provided its own in-house administrative support independent of the Department. Accordingly, the office’s administrative specialists provided a wide range of administrative services, including budget, accounting, procurement, facilities, human resources, and information technology. With our post divestiture staffing level of 87 FTE we can no longer sustain an in house administrative support function. We are divesting over 75 percent of our support staff to the DHS OIG.

Post-divestiture, the Office of Management is revamping its approach to administrative support. Specifically, we are in the process of contracting with service providers for assistance with procurement, accounting, facilities management, recruitment, processing of personnel actions, and IT support. These changes in the OIG support infrastructure will allow the Office of Management to continue to provide support services to investigators and auditors with a minimum of in house staffing.

MANAGEMENT AND PERFORMANCE CHALLENGES

On November 5, 2002, we provided the Secretary of the Treasury a summary of the most serious management and performance challenges facing the Department. That memorandum was included in the *Department of the Treasury Performance and Accountability Report for Fiscal Year 2002.* I would like to highlight five of these challenges for purposes of this testimony. I also want to point out that except for one new challenge—that dealing with the need to ensure a smooth transition of activities to Homeland Security—the following challenges were reported to the Secretary in the previous year and while some progress had been made, they still must be overcome to realize the goals and objectives of the President's Management Agenda. Also, while Treasury’s divestiture of most of its law enforcement functions will change the scope and magnitude of these challenges, it does not eliminate any of them. We will need to maintain our oversight of Treasury’s efforts to manage these challenges going forward.

- <u>Prompt Corrective Action</u> – Treasury has not taken sufficient action to address longstanding material weaknesses and other serious deficiencies in programs and operations. While some of these material weaknesses are attributable to divested bureaus, notably Customs, others remain, including information security and other systems weaknesses and the Department's ability to properly prepare the financial statements for the Federal government.

- <u>Linking Resources to Results</u> – Very little progress has been made by Treasury to integrate managerial cost accounting into its business activities; thus, resources cannot be linked to results. This undermines the accuracy, reliability, and usefulness of program performance reporting and precludes meaningful cost benefit analysis of the Department's program activities.

- <u>Financial Management Systems</u> – Treasury continues to operate financial management systems that are not capable of producing timely, accurate, and reliable information although some progress has been made as evidenced by the "3-day close" initiative for monthly financial reporting and the accelerated financial reporting for fiscal year 2002. However, these data needs to be reviewed, analyzed, refined, and correlated with other financial and non-financial data in order to be reliable and useful.

- <u>Information Security</u> – Treasury has not corrected longstanding information security problems. Our work under GISRA last year disclosed numerous vulnerabilities that had not received adequate attention. Most of the Department's systems at the time had been allowed to operate without a reasonable assurance of secure operations or adequate safeguards. Only 32 percent of the Department's systems were accredited, including 9 percent that only had interim authority to operate.

- <u>Duplicated, Wasteful Practices</u> – Treasury has not adapted enterprise solutions to its core business activities. Thus, rather than realize the economy, efficiency, and effectiveness of consolidation and sharing, Treasury bureaus and offices continue to operate as autonomous agencies.

Finally, as you can see from my description of the Department post divestiture, there are many significant activities beyond these broad management challenges that will require our oversight. Just to highlight a few, Treasury maintains an important role to play in the war on terrorism, with the efforts to disrupt and dismantle the mechanisms that support terrorist financing. Over $15 billion in non-IRS revenue will still be collected and accounted for in the new Tax and Trade Bureau. It will need to continue to operate effectively in a new environment, separated from the rest of the old ATF. Treasury is at the forefront in developing e-government initiatives, especially in the payment systems at FMS, the debt financing systems at BPD, and the online sales systems at the Mint. While they help make those operations more efficient and more available to the public, they come with an increased risk for major security vulnerabilities and major system failures that require sound disaster recovery capabilities. The two Treasury bank regulators, OTS and OCC, oversee all thrifts and over 58 percent of the commercial banks in the United States. This represents financial institutions with close to $1.4 trillion in assets. With prolonged weakness in the economy, the risk of bank and thrift failures remains a concern and OCC and OTS will need to maintain strong oversight of their institutions.

We will need to maintain a reasonable level of audit and investigative capacity to help ensure the public that these and other Treasury programs and operations are delivered efficiently and effectively, and with the highest level of honesty and integrity.

This concludes my testimony. I will be happy to answer any questions at this time. Thank you.