STATEMENT OF JEFFREY RUSH, JR.

INSPECTOR GENERAL

DEPARTMENT OF THE TREASURY

BEFORE THE HOUSE COMMITTEE ON APPROPRIATIONS

SUBCOMMITTEE ON TREASURY, POSTAL SERVICE, AND GENERAL GOVERNMENT

MARCH 21, 2001

Chairman Istook, Ranking Member Hoyer, members of the subcommittee and subcommittee staff - Good morning.

This is my first opportunity to appear before this subcommittee. I am delighted to be here this morning to testify about the organization, staffing, mission and challenges facing the Office of Inspector General, Department of the Treasury.

I am also pleased to be here with Inspector General David C. Williams, the Treasury Inspector General for Tax Administration. As you know, the Treasury Department is the only cabinet agency with two Inspectors General. It is ironic that for more than a decade after the Inspector General Act of 1978 was passed, four administrations argued against establishing a single OIG for the Department. Now Treasury has two.

While the balance of my testimony will focus on where we are today and where we are going, I want to make one brief comment about the recent past.

This organization, since it became a statutory IG, has seen a great deal of change in the leadership and has undergone a period of turmoil. The conduct of several officials of the Treasury OIG was the subject of investigation by the Permanent Subcommittee on Investigations of the Senate Government Affairs Committee, the U.S. General Accounting Office, and the President's Council on Integrity and Efficiency.

Between February 1998 and July 1999 the workforce was led by three different Senate-confirmed IGs and an acting IG. Through all of this, the career staff stayed focused on the core mission of conducting independent and objective audits and investigations. I am impressed with their accomplishments.

I believe the Treasury OIG is stronger now than it has ever been and that we are moving in the right direction to meet the challenges that will face the Department over the next decade.

My testimony will be presented in two parts. Part I will cover our current organization, staffing and mission. Part II will cover the significant issues facing the Department of the Treasury, what we have to do to address them, and what initiatives we have underway to continue improving our own capacities. And, to give this committee some additional background, I have also attached a history of the Treasury OIG prior to its establishment by statute. (Attachment 1).

As you know, the Department of the Treasury was created by Act (1 Stat.65) on September 2, 1789. The Department is comprised: (1) **Departmental Offices,** (2) **Treasury Forfeiture Fund,** (3) **Exchange Stabilization Fund,** (4) **Federal Financing Bank,** (5) **Financial Crimes Enforcement Network,** and (6) **Community Development Financial Institution Fund**.

The Department also has eleven bureaus (not including OIG and TIGTA): (1) **Bureau of Alcohol, Tobacco, and Firearms (BATF),** (2) **U.S. Customs Service (USCS),** (3) **U.S. Secret Service (USSS),** (4) **Federal Law Enforcement Training Center (FLETC),** (5) **Financial Management Service (FMS),** (6) **Bureau of Public Debt (BPD),** (7) **U.S. Mint (Mint),** (8) **Bureau of Engraving and**

Printing (BEP), (9) **Comptroller of the Currency (OCC)**, (10) **Office of Thrift Supervision (OTS)**, and (11) **Internal Revenue Service (IRS)**. My office is responsible for supervising or conducting the audits and investigations relating to all of the bureaus and offices, except the **IRS**.

Our universe of audits, evaluations, and investigations involve more than 47,500 Treasury employees who provide a wide range of services throughout the United States and from an increasing number of foreign cities. The following key statistics show the scope and variety of the Department's programs and operations. This information is for FY 2000 except where noted.

- **Customs** collected $24 billion in duties and other revenue and paid $1.2 billion in refunds and duty drawback. It processed 23.4 million trade entries and 489 million travelers entering the United States. During the fiscal year, the value of imports totaled $1.17 trillion. **Customs** is also undertaking a major system initiative, the Automated Commercial Environment, to replace its current, outdated trade system.

- **ATF** collected $14.1 billion generated by Federal excise taxes on alcohol, tobacco, firearms, and ammunition. It also expended $447 million for various programs directed at reducing violent crimes, such as the Youth Crime Gun Interdiction Initiative.

- **FMS** issued over 890 million payments, totaling more than $1.2 trillion. About 70 percent of these payments were electronic.

- The Department, through **BPD**, issued about $2 trillion of securities, most of which was done to replace maturing securities. It also reintroduced the buyback of outstanding Treasury securities for the first time in 70 years. BPD conducted 13 buyback operations, repurchasing over $21 billion.

- The **Mint** produced 56.1 billion coins. During FY 1999, the latest information available, **BEP** delivered 11.4 billion Federal Reserve Notes and 19 billion postage stamps.

- As of September 30, 2000, **OCC** has 2,242 national banks under supervision with total assets of $3.4 trillion. **OTS** has 1,082 thrifts under supervision with total assets of $908 billion.

- The Department and its bureaus operate more than 900 information systems. More than 250 are considered mission-critical.

- Procurements by the Department and its bureaus, totaled an estimated $1.8 billion.

PART I - ORGANIZATION, STAFFING AND MISSION OF THE OIG

The Treasury OIG was established in 1989 by the Secretary 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 the Treasury Inspector General for Tax Administration. That office was established as a result of the Internal Revenue Service Restructuring and Reform Act of 1998.

The OIG is headed by an Inspector General who is appointed by the President with the advice and consent of the Senate. Serving with the Inspector General in the immediate office is a Deputy Inspector General. The Deputy Inspector General is a career employee and a member of the Senior Executive Service. The Deputy Inspector General shares responsibility for the leadership of the OIG workforce and management of the OIG's resources. The OIG is organized into four components: audit, investigations, management services, and legal counsel.

Attached are the following:

-- Organizational Table (Attachment 2);
-- Staffing Table for Fiscal Years 2001 and 2002 (Attachment 3);
-- Map showing field offices and regional boundaries (Attachment 4).

OIG Audit

The Office of Audit is the largest component in my office. It is led by the Assistant Inspector General for Audit. There are two major functions in the Office of Audit, financial audit and program audit, each under the leadership of a Deputy Assistant Inspector General for Audit. The Office of Audit also has an evaluations group.

The financial audit staff was created in 1994 to meet our obligations under the Chief Financial Officer (CFO) Act and the Government Performance and Results Act (Results Act). The Treasury Department, is responsible for collecting 98% of the revenue, managing the $5 trillion debt and performing the central accounting functions for the federal government. We made a major internal reallocation of staffing to create the infrastructure and develop the expertise to perform the audits required by this legislation. Within two years, we had one of the strongest financial auditing capabilities within the IG community. We continue to maintain and strengthen that capacity.

The financial audit staff also manages our information technology auditing resources. They support the automated data processing general control work that is done as part of the annual financial statement audits. They also conduct audits of major information technology (IT) acquisitions, information security, and compliance with major IT legislation such as the Computer Security Act and the Information Technology Management Reform Act (Clinger Cohen). They will also be our focal point for meeting our new requirements under the Government Information Security Reform Act.

The program audit staff is responsible for conducting economy, efficiency and effectiveness audits for all Treasury bureaus and operations except the IRS. The highly diverse nature of the Treasury missions make this a very challenging audit environment. We need to maintain knowledge and expertise in areas that include law enforcement, manufacturing, banking regulation, trade enforcement, fiscal services and debt management. We accomplish this with a structure that includes four Regional Inspectors General for Audit located in San Francisco, Houston, Chicago and Boston and three Directors of audit in Washington, D.C. While these groups can perform audits of any Treasury activity, they each have primary responsibility for maintaining current knowledge in one of those Treasury missions.

Finally, the Office of Audit includes an evaluations unit. This group performs special management studies and reviews that are more effectively performed outside of the traditional audit discipline. For example, they were our focal point for our early work in helping the Department and bureaus establish their processes and procedures to comply with the Results Act.

OIG Investigations

The Assistant Inspector General for Investigations (AIG/I) is responsible for supervising and conducting investigations of the Department's programs and operations and exercising oversight activities on the inspections and internal affairs units of three law enforcement bureaus.

OI is responsible for the prevention, detection and investigation of any apparent violation of rule, regulation, or law in connection with Treasury programs and operations. The OI provides direct oversight of the internal investigations performed by the Office of Inspections of the **Bureau of Alcohol, Tobacco and Firearms**, the United States **Customs** Service, and the Office of Internal Affairs of the United States **Secret Service**.

Types of investigations conducted by OI include allegations of corruption, procurement fraud, false claims, serious employee misconduct or other illegal acts. OI receives and investigates complaints or information received from employees, contractors, and other individuals alleging violations of the law, rules, or regulations.

A Special Agent in Charge heads the Enforcement Operations Division (EOD). EOD is responsible for the administration of the OI budget and records management. It is also responsible for developing OI policy and procedures, developing an ongoing training program and maintaining the Victim/Witness Protection and Special Agent deputation programs.

Under the umbrella of EOD is the Operations Control Unit (OCU) which is responsible for the Treasury OIG Hotline. OCU also receives and processes all allegations and correspondence received by OI. OCU manages the Investigations Database Management System (IDMS) which tracks and monitors all activities relating to investigations and information data requests received within OI.

The Treasury Integrity Division (TID) is supervised by a Special Agent in Charge. TID is comprised of the Special Investigations Unit (SIU) and the Treasury Inspection Unit (TIU).

TIU has the primary responsibility of providing liaison and oversight activities of all of the Department's bureaus, including the internal affairs functions of three of the Department's law enforcement bureaus. TIU is also responsible for the review and referral of all allegations to OI Field Offices or Treasury Bureaus for investigation or management action, and the internal inspection program of the OI field offices.

The SIU is responsible for investigating allegations against Department bureau heads and Treasury senior executives. Additionally, SIU investigates complaints received from members of Congress and conducts other investigations deemed sensitive to the Department.

Field Offices

There are five Field Offices and two sub-offices within OI, each supervised by a Special Agent in Charge. These offices are responsible for conducting investigations into allegations of criminal and other serious misconduct by Treasury employees and contractors. The field offices undertake the responsibility and initiative to develop proactive investigative initiatives; conduct fraud awareness briefings of Treasury employees; and coordinate liaison activities with other law enforcement officials within their region of responsibility. The five field offices are located in San Francisco, CA; Chicago, IL; Houston, TX; Marlton, NJ; and Alexandria, VA; and the two sub-offices are located in Los Angeles, CA; and Miami, Fl.

Investigative Priorities for FY 2001/2002

OI has established several priorities relating to its overall initiatives for FY 2001/2002.

- We have developed OI's computer forensic capabilities by training special agents on computer and data recovery techniques to ensure they are prepared to meet the challenges in conducting computer crime investigations, and information security assessments.

- We are continuing to expand OI's oversight of the Department's law enforcement bureaus internal affairs components. During FY 2000 the Treasury Inspection Division (TID) examined over 600 reports of investigation conducted by the internal affairs functions of the law enforcement bureaus. These reviews were undertaken to determine if allegations of misconduct were conducted thoroughly, impartially and timely. Additionally, TID reviewed over 260 discipline files to ensure that the bureaus administered discipline fairly and equitably.

OIG Management Services

The Assistant Inspector General for Management Services is responsible for providing the technical, financial, and administrative infrastructure to the Office of Inspector General. The office is responsible for internal policies and procedures, special projects, statistical analysis services and database administration.

The Director of Administrative Services oversees the administrative support for the OIG staff. This includes direction for the travel program, issuance of credentials, records management, space planning and acquisition, procurement and contract actions for goods and services, and support services for the OIG field offices.

The Budget Officer provides financial management services. The budget execution function involves managing the annual funding allocations, tracking and analyzing spending patterns, processing financial documents, and reporting on the use of resources. The budget formulation function involves developing, justifying and presenting future year budget requests to the Department, the Office of Management and Budget, and the Congress.

The Personnel Officer heads the Human Resources Office (HR) which provides a full-service human resources program to the

OIG and its employees. HR is responsible for providing all services for recruitment and staffing, position classification and position management, employee relations and performance management, awards and recognition, employee development, benefits, and payroll processing.

The Office of Information Technology is responsible for installing, supporting, maintaining, and managing all IT hardware and software and the telecommunications used to support the OIG staff and operations.

Information Technology

In FY 2000, the OIG established an Information Technology Advisory Committee made up of users of our information technology. In addition, we contracted for an assessment of our IT infrastructure. Based on recommendations from the Committee and the assessment, we developed a process to evaluate recommended changes to IT, to assure that they support our business processes. We are currently installing new servers and computers to better serve our employees.

OIG Counsel

The Counsel to the Inspector General serves as the senior legal and policy advisor to the Inspector General, Deputy Inspector General, and the Assistant Inspectors General. The Counsel has responsibility for all legal work in the Office of Inspector General.

The Office of Counsel, which is located in Washington, D.C., provides legal advice on issues arising during the course of the statutorily mandated investigative, oversight, and audit activities conducted by the Offices of Investigations and Audit. In addition, the Office of Counsel provides legal advice on issues concerning government contracts, appropriations, budget formulation and execution, disclosure, records retention, tax information safeguards, equal employment opportunity, and personnel law. The office represents the OIG in administrative proceedings before the Merit Systems Protection Board and the Equal Employment Opportunity Commission.

The office is also responsible for managing the OIG ethics program, which includes ensuring compliance with financial disclosure, providing training, and rendering advice on the governing laws and regulations. In the area of disclosure law, the Office of Counsel manages the OIG's Freedom of Information Act (FOIA) and Privacy Act programs. The Office of Counsel also coordinates document requests from Congress and in connection with litigation, and responds to Giglio requests from the Department of Justice for information on Treasury law enforcement agents, who will serve as witnesses in criminal trials.

Activities in Fiscal Year 2001/2002

The Office of Counsel will continue to provide training on the Inspector General Act. Treasury Order 114-01 and Treasury Directives 27-12 and 40-01 will be revised to reflect current structure and responsibilities and the publication of these documents will be coordinated through the Department of the Treasury. As statutorily mandated, legislative and regulatory proposals will be reviewed and, where appropriate, comments will be coordinated.

In the area of disclosure, the Office of Counsel will implement an independent FOIA and Privacy Act program for the OIG. Based upon past experience, the Office of Counsel expects to process 90 initial FOIA/Privacy requests and 30 appeals from those initial responses. In the area of electronic FOIA, the Office of Counsel expects to review 125 audit reports for posting on the OIG web site. The Office of Counsel will complete amended Privacy Act systems of records notices for both OIGs investigative and administrative records systems.

PART II - MANAGEMENT AND PERFORMANCE CHALLENGES AND MANDATED WORK

On February 28, 2001, I provided the Secretary a summary of the most serious management and performance challenges facing the Department. That memorandum (Attachment 5) was included in the *Department of the Treasury Accountability Report for Fiscal Year 2000*. While each of these areas are significant, I would like to highlight four for purposes of this testimony and discuss work we have performed and plan to perform to provide oversight of Treasury's performance.

One of the major challenges we identified is the need to improve financial management. Treasury has made steady progress in this area, and for the first time we issued an unqualified opinion on Treasury's consolidated financial statement. While this is a significant achievement it represents only an interim milestone. Treasury can only achieve this by performing costly and extensive manual efforts, which compensate for material weaknesses and automated systems that do not comply with the Federal Financial Management Improvement Act requirements. The ultimate goal of producing timely reliable financial data that can be used to improve accountability and decision making has yet to be achieved.

We have continued to make a major resource commitment to provide the independent audits, which are required in order for the Department to comply with the CFO Act and the Government Management Reform Act. We are responsible for issuing fifteen individual entity audit opinions in addition to the Treasury consolidated opinion. However, we have done much more than just perform the independent audits. We have helped management find solutions to correct material weaknesses and to address unique accounting issues that have continually arisen from the diverse and complex financial responsibilities that reside in Treasury. We have also coordinated with the GAO to avoid duplication and effectively leveraged resources to ensure that those Treasury entities and accounts that are material to the government-wide financial statement are sufficiently audited.

Information security is another major area of vulnerability for the Department, as it is for most federal agencies. It used to be that it would require a massive failure or attack on physical plant and equipment to bring an agency to its knees. Today it can be accomplished with little more than a few keystrokes. The ability to recover from a disaster is just as critical as the ability to prevent one, maybe even more critical. Yet it is one of the most vulnerable areas for many agencies. Last year, I took the somewhat rare step of issuing a "7-day" letter to the Secretary to highlight a very serious vulnerability at **Customs** involving disaster recovery and continuity of operations. While this represents one of the more serious weaknesses in information security at Treasury, many other systems also have significant weaknesses.

Information security has been and will continue to be a priority area for our IT audit program. We currently have eight audits in this area in our Fiscal Year 2001 audit plan. The recently enacted Government Information Security Reform Act now requires us to perform an independent annual evaluation of the Department's information security program. We are working with the Treasury CIO to see how we can integrate the work we currently perform into the work we will need to perform to meet this mandate.

The safety and soundness of financial institutions is a third major challenge I want to highlight. As mandated by law, we reviewed **OCC's** supervision of the First National Bank of Keystone in West Virginia, which had failed and cost the bank insurance fund over $700 million. We concluded that the Keystone failure offered several valuable lessons and opportunities for **OCC** to improve examinations and enforcement procedures. For example, we recommended that **OCC** evaluate whether a different supervisory approach is needed for banks with rapid growth in high-risk activities, even when accompanied by high profitability and adequate capitalization. We also conducted an audit to look at **OCC's** supervision of banks selling insurance, an emerging new area of banking powers that can pose additional risks to safety and soundness. Among other things, our report pointed out that undue reliance on state functional regulators, or any third party for that matter, may not be prudent.

The last management challenge I will discuss is revenue protection by **Customs** and **ATF**. One result of the financial statement audits of **Customs** over the years is that the bureau has implemented a statistical methodology to annually project the "revenue gap" from non-compliant importers. This measurement program can provide useful information to **Customs** in its efforts to improve compliance. We have also performed a number of program audits that have identified areas where improvements in controls affecting revenue collection need to be made such as in **Customs**' Air Manifest System and **ATF's** processing of tax-free exports of spirits and tobacco products.

In closing, I would like to briefly discuss a matter of increasing concern in my office and in some other offices of Inspectors General. I have compiled a list (Attachment 6) of fourteen Federal statutes that in some way attempt to reform or improve the performance of government agencies and operations. Each of the statutes mandates or requires some action by my office.

These mandates, particularly those involving the audit of financial statements, and information management and security, occupy over one-half of our audit resources. They limit my ability to independently establish the priorities of the OIG, and restrict our responsiveness to emerging issues that can affect the Department's accomplishment of its missions.

I believe that the utility of some of these requirements to improve management, accountability, and program effectiveness should be evaluated to determine if they still add value.

Thank you.

ATTACHMENT 1 - HISTORY OF THE TREASURY OIG

ATTACHMENT 2 - OIG ORGANIZATIONAL CHART

ATTACHMENT 3 - OIG STAFFING TABLES FOR FY 2001 AND FY 2002

ATTACHMENT 4 - MAP SHOWING OIG FIELD OFFICES AND REGIONAL BOUNDARIES

ATTACHMENT 5 - MEMORANDUM TO SECRETARY O'NEILL, SUBJECT: MANAGEMENT AND PERFORMANCE CHALLENGES

ATTACHMENT 6 - FEDERAL STATUTES THAT IMPACT OIG WORKLOAD AND PRIORITIES

HISTORY OF THE OIG

To provide the committee with a brief history of our office, I will rely on the August 1986 report of the U.S. General Accounting Office, Treasury Department, *An Assessment of the Need for a Statutory Inspector General*. I will quote from that report on pertinent part.

Treasury Exempt for Inspector General Act of 1978

"During 1977 congressional hearings on the need for a statutory IG at Treasury, department officials cited Treasury's unique role, especially its law enforcement and monetary policy roles, as reason for not being included under the act. Congress agreed to study the issue further and did not include Treasury among those agencies covered by the 1978 legislation.

In 1982, the Comptroller General wrote to the chairman of the Senate Committee on Governmental Affairs in support of legislation which, among other things, would have established a statutory Inspector General at Treasury. The Comptroller General noted that to be fully effective, a statutory Office of Inspector General should fulfill two primary objectives:

- be as independent as possible from agency management control over audit and investigative operations, and
- report particularly serious problems to the head of the agency and the Congress.

Treasury's Internal Audit and Investigations Functions

In 1978, the Secretary of the Treasury administratively established the position of Inspector General, but the responsibilities of the position were limited. Since then, the Department has expanded the Inspector General's role to include audits and investigations in the non-law enforcement bureaus and offices. However, that gave the Inspector General direct authority for auditing and investigating only 11 percent of Treasury's fiscal year 1985 budget authority and 7 percent of the authorized staff.

The Department authorized the Office of Inspector General a budget of $4.9 million and 119 staff positions for fiscal year 1985. The IG's staff was located in Washington, D.C., except for one auditor at the Federal Law Enforcement Training Center in Georgia and small staffs in three Bureau of the Mint locations and in one Bureau of Public Debt office.

The four law enforcement bureaus have retained their own internal audit and investigative staffs. The Department has proposed further consolidation of the audit functions under the Inspector General. However, language included in Treasury's appropriation legislation since 1982 has precluded the use of any funds to place the law enforcement bureaus 'under the operation, oversight, or jurisdiction' of the Inspector General.

Treasury's Non-statutory Inspector General

The Treasury Inspector General reported directly to the Secretary and Deputy Secretary. Initially, the Inspector General was authorized to conduct investigations within the Office of the Secretary and those investigations which bureaus and offices did not wish to perform using their own resources.

The Office of Audits was transferred to the Inspector General in 1980, giving the Inspector General responsibility for audits within the Office of the Secretary. In the same year, a Treasury directive gave the Inspector General oversight responsibility for all audits and investigations within the Department. The Inspector General was authorized to:

- provide advice and assistance to bureaus and offices;
- review and approve bureau and office annual audit and investigative plans for adequacy in ensuring the highest standards of integrity;
- conduct periodic oversight reviews of internal audit and investigative activities for objectivity, thoroughness, and effectiveness;
- investigate allegations involving senior officials of any Treasury office or bureau;
- participate in the selection of key internal audit and investigative positions; and
- prepare an annual report of all internal audit and investigations activities in the Department.

In 1982, Treasury proposed a major reorganization of its audit and investigative staffs. The Secretary planned to consolidate all audit and investigative staffs from the non-law enforcement bureaus and the audit staffs from three law enforcement bureaus (Customs Service; Bureau of Alcohol, Tobacco and Firearms; and Secret Service) under the Inspector General. Fifteen investigator positions were also to be transferred to the Inspector General from the three law enforcement bureaus, although these three bureaus would retain responsibility for conducting their own internal investigations.

Under the Department's planned consolidation, the Internal Revenue Service (IRS) was to be the only bureau within the Department to retain its audit and investigative staff intact. In a memorandum to the Secretary, Treasury's Inspector General stated that departmental management had considered including the IRS audit function under the Inspector General but decided it was inadvisable at that time. The Inspector General said the decision had been made because:

- the Congress had consistently excluded IRS from the bills establishing a statutory, consolidated OIG;
- the IRS audit function had been statutorily created in 1951 and, therefore, bore a different relationship to IRS and to the Department than did the other inspections units;
- the size of this unit would have made the consolidation more difficult administratively; and
- the OIG had oversight responsibility for the internal audit and investigative functions within IRS.

When members of the House and Senate appropriations subcommittees were informed of the consolidation plan, they expressed concerns about the advisability of including the three Treasury law enforcement bureaus (Customs, Secret Service, and BATF) in the consolidation. Specifically, the subcommittee chairmen noted concerns about confidentiality of Secret Service protective activities and of narcotics and firearms investigations conducted respectively by the Customs Service and BATF. The chairmen expressed concerns that freedom-of-information requests could lead to disclosure of sensitive information. They also noted that law enforcement agencies have institutional experience that Inspector General offices do not.

A provision was included in Treasury's supplemental appropriation for fiscal year 1982 prohibiting the use of any funds to place the three law enforcement bureaus "under the operation, oversight, or jurisdiction" of the Inspector General. Although Treasury has opposed the language, the same provision has been included in subsequent Treasury appropriation legislation.

Consequently, the only portion of the proposed 1982 reorganization, which was carried out, was the consolidation of the audit and investigative resources of the non-law enforcement bureaus under the Office of Inspector General. This gave the OIG the direct audit and investigative responsibilities that it now has for only 11 percent of the Department's fiscal year 1985 budget authority. The Inspector General retained oversight responsibility for the audit and investigative offices in law enforcement bureaus as directed in 1980. In addition to their established bureau reporting responsibilities, the heads of the audit and investigative staffs in each of the law enforcement bureaus report to the Inspector General for oversight purposes.

When a newly appointed IG assumed his duties in 1984, he questioned his oversight authority for the law enforcement bureaus in view of the language in Treasury's appropriations legislation. The IG counsel responded that "as oversight arrangements already existed and no funds were (or are) necessary to facilitate transfer of these monitoring functions, existing oversight authority remains unaffected by this or any similar statute." The IG has exercised his oversight responsibilities as provided in the 1980 Treasury directive and has received the cooperation of law enforcement bureaus' internal affairs/inspection offices in conducting departmentwide audits and detailing staff to the OIG when needed.

If the Department were able to complete the consolidation as proposed in 1982, the Inspector General would gain direct internal audit responsibility for the BATF, Customs Service, and Secret Service. IRS, which accounts for 67 percent of Treasury's budget and 76 percent of the authorized staff, would retain its own internal audit and investigation staff subject to IG oversight. Any plan for consideration, which does not include the IRS, would only give the IG audit and investigative responsibility for less than one-third of Treasury's resources.

Audit and Investigations Offices in Law Enforcement Bureaus

The four law enforcement bureaus - Bureau of Alcohol, Tobacco and Firearms; Internal Revenue Service; Customs Service; and Secret Service - each had its own office of internal affairs/inspections, which is responsible for internal audits and investigations within its respective bureau. The head of each of these offices reported to the respective bureau director/commissioner. These bureaus have historically operated somewhat autonomously of the Department. This autonomy appeared to be at least somewhat supported by language in appropriation legislation, which has prevented the Inspector General from assuming responsibility for audits in these bureaus.

Each of the internal affairs/inspection offices was organizationally part of the bureau which it audits. In three bureaus (BATF, IRS, and the Customs Service), staff is permanently assigned to the internal audit and investigative unit, with promotion and other personnel decisions made within the internal affairs office. Each of these offices plans its audit work based on audits required by law and on input from bureau management, auditors, and the Treasury Inspector General. The investigation staffs are primarily reactive groups, which respond to allegations of misconduct involving bureau personnel.

The Secret Service Office of Inspections differed from the other three bureaus in staff assignment. This office ha 26 investigators who served rotational assignments of 1 to 2 years as part of their management development process. Four auditors, who composed the balance of the staff, are permanently assigned. The investigators perform internal investigations based on allegations of misconduct and inspections of Secret Service field offices and divisions throughout the country. The primary purpose of these inspections is to determine if procedures were being followed, to evaluate Secret Service relations with local law enforcement authorities, and to assess office morale. Investigators assigned to the Office of Inspections apply for promotions in divisions and field offices as vacancies occur; therefore, it was possible for an investigator to apply for promotion in an office after conducting an inspection of that office. The Assistant Director (Inspection) was not aware of any conflict that has occurred as a result of this process.

reports prepared by the internal affairs/inspection offices were issued to the director of the particular section or program being reviewed, or to the bureau director. A Treasury directive required the director of each internal affairs/inspection office to report back to the IG on all investigations referred by the IG plus audits and conducts other investigations, which he/she believes to be significant. In addition, the internal audits office directors were expected to cooperate in preparing the IG's annual report to the Secretary. No specific provisions existed for reports to be sent directly to the Secretary or Deputy Secretary.

The individual law enforcement bureaus determine the level of resources for their respective internal affairs offices. In addition to the staffs located in Washington, D.C., the Customs Service had auditors and investigators in seven regional offices, and BATF has investigators in three regions.

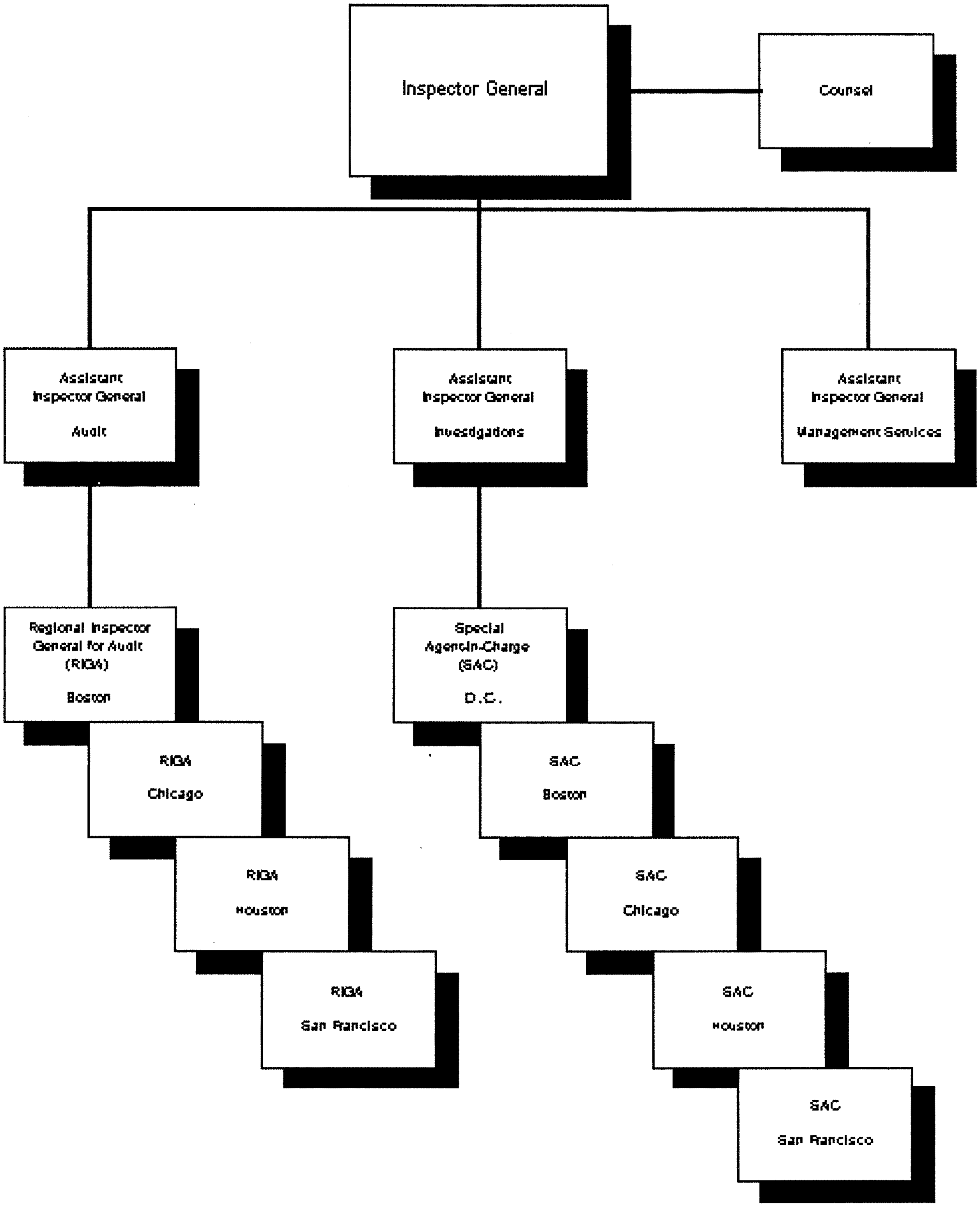
Treasury's Audit and Investigations Structure Differs from IG Act Requirement

Treasury's current organizational structure for internal audits and investigations differed significantly from requirements of the IG Act. Rather than having an Inspector General as the central leader for audits and investigations, Treasury's IG had been given limited audit and investigative responsibilities. The majority of the Department's resources are subject to audit and investigation by internal affairs/inspection offices organizationally within the four law enforcement bureaus. This structure did not provide the degree of independence to auditors and investigators envisioned by the IG Act. The Inspector General's oversight responsibilities for audits and investigations in the law enforcement bureaus has been subjected to question by language in the Department's appropriation legislation.

The IG Act states that those agencies covered by the act shall have an Inspector General "to provide policy direction for and to conduct, supervise and coordinate audits and investigations relations to the programs and operations" of the agency. The Inspector General is to be the focal point of these activities for the entire Department. If Treasury were included under the

Inspector General Act of 1978, without modification, the IG would have direct responsibility for conducting audits and investigations in all of Treasury's bureaus and offices.

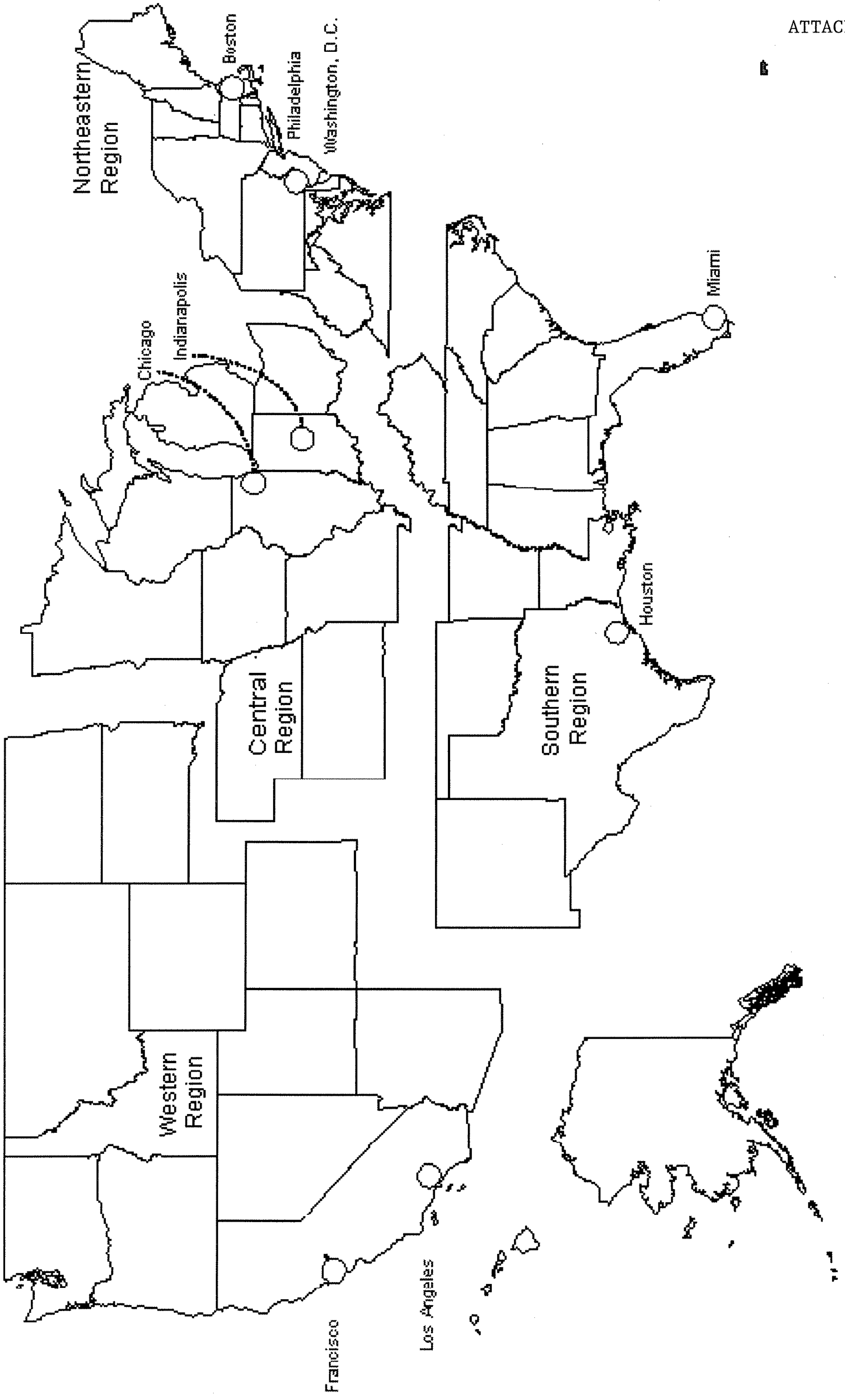
The act required statutory Inspectors General to keep the agency head and the Congress 'fully and currently informed' concerning fraud and other serious problems, abuses, and deficiencies. Treasury's administrative Inspector General is unable to keep the Secretary informed since the Inspector General does not receive copies of all audit reports issued by the law enforcement bureaus' internal affairs/inspection offices. In addition, the internal affairs/inspection offices are not required to report to the IG on investigations that are self-initiated or result from internal allegations. Treasury's Inspector General was not required to report to the Congress."


Inspector General
Counsel
Assistant Inspector General Audit
Assistant Inspector General Investigations
Assistant Inspector General Management Services
Regional Inspector General for Audit (RIGA) Boston
RIGA Chicago
RIGA Houston
RIGA San Francisco
Special Agent-in-Charge (SAC) D.C.
SAC Boston
SAC Chicago
SAC Houston
SAC San Francisco

OIG STAFFING ALLOCATIONS
(Full-time Equivalent Positions)

	Fiscal Year 2001	Fiscal Year 2002
Immediate Office	5	5
Counsel	7	8
Management Services	30	32
Investigations	70	72
Audit	160	165
Total	272	282

ATTACHMENT 4



ATTACHMENT 5

DEPARTMENT OF THE TREASURY
WASHINGTON

INSPECTOR GENERAL

February 28, 2001

MEMORANDUM FOR SECRETARY O'NEILL

FROM: Jeffrey Rush, Jr.
Inspector General

SUBJECT: Management and Performance Challenges Facing the Department of the Treasury

SUMMARY

The Reports Consolidation Act of 2000 requires that we provide you with our perspective on the most serious management and performance challenges currently facing the Department of the Treasury for inclusion in the *Department of the Treasury Accountability Report for Fiscal Year 2000*. This new legislation codified into law what had become, since 1997, an annual request of my office from the Senate and House leadership for similar information.

In our December 2000 response to the Congress, we identified nine serious challenges. The following eight challenges were identified in our prior year response: (1) Information Security, (2) Treasury's Information Technology Investment Management, (3) Money Laundering/Bank Secrecy, (4) Narcotics Interdiction and Trade Enforcement, (5) Revenue Protection, (6) Violent Crime, (7) Implementation of the Government Performance and Results Act, and (8) Financial Management at Treasury/Compliance with the Federal Financial Management Improvement Act. While Treasury has made substantial progress to address these challenges, we were not able to remove any from our December 2000 list because each continues to present a serious risk. In addition, we identified the following new challenge for 2000: Safety and Soundness of the Banking Industry.

It should be noted that Treasury made sufficient progress in addressing certain other previously reported serious challenges to warrant their removal from our list. These challenges include (1) Year 2000 compliance, (2) Treasury's debt collection initiatives, and (3) Electronic Funds Transfer/ Electronic Benefits Transfer.

The Treasury Inspector General for Tax Administration will separately address challenges related to the Internal Revenue Service (IRS).

DISCUSSION

Our reasons for identifying these nine challenges as the most serious facing Treasury are as follows:

1. Information Security

Protecting information and data from unauthorized access is critical to ensure, among other things, the integrity of Treasury's law enforcement and financial operations. Information technology (IT) enables Treasury to achieve its business goals but creates a number of internal control challenges. As information becomes more accessible through electronic means, threats to security increase. This has given rise to various initiatives to improve the Government's infrastructure.

Treasury has achieved some of its security goals such as establishing an Information System Architecture Framework and Public Key Infrastructure draft standards. However, more needs to be done.

Our audits have found significant, long-standing weaknesses in the U.S. Customs Service's (Customs) ability to maintain continuity of operations as well as overall security and access control. As a result, we issued a "7-Day" letter to the Secretary of the Treasury on May 26, 2000, who in turn notified Congress as required by the Inspector General Act. In that letter, we recommended that Customs take immediate steps to develop an alternative site for continuity of operations and install firewall and detection software to reduce the risk of unauthorized Internet access. Our audits have also identified Electronic Data Processing general control weaknesses at other Treasury bureaus, most notably the Financial Management Service (FMS). We also found that Treasury needed to devote additional resources to its implementation of Presidential Decision Directive (PDD) 63 which requires the development of a reliable, interconnected, and secure information system infrastructure. Treasury's efforts to implement PDD 63 have revealed the lack of resources being devoted to the effort. Furthermore, we noted the need for Treasury to identify and prioritize its critical assets.

2. Treasury's Information Technology Investment Management

The Clinger Cohen Act of 1996 (CCA) sets the groundwork for effective management of IT investments. With nearly $2 billion annually invested in IT by Treasury, CCA requires improved capital planning, investment controls, project management, systems development, and performance measurement. Treasury's weaknesses in effectively managing major IT investments have been well documented over the past several years for such systems as the IRS Tax System Modernization and the Customs Automated Commercial Environment (ACE) initiative. We recently issued a report detailing Treasury's implementation of CCA. In that report, we noted that the Treasury Investment Review Board (IRB) and Departmental practices needed improvement if they were to be able to provide executive direction and effective management over IT investments. Treasury implemented some CCA requirements and a number of our recommendations. Two examples of this are the restructuring of the IRB and expanded IRB oversight of 14 capital investment projects.

3. Money Laundering/Bank Secrecy

It is estimated that criminals launder hundreds of billions of dollars globally each year. It was recently reported that Citibank, the nations largest bank, failed to follow Federal guidelines to prevent money laundering and allowed as much as $800 million in suspicious Russian funds to flow through 136 accounts. In an audit we performed on the Office of the Comptroller of the Currency's (OCC) Bank Secrecy Act (BSA) examinations, we identified the need for OCC to strengthen examination procedures in several areas. We found that OCC examiners did not always perform complete BSA examinations including (1) following up on indicators of suspicious activity and (2) performing sufficient reviews of high-risk accounts. OCC agreed to take a number of actions, which should improve BSA examinations. Our work on Customs' strategic money laundering initiatives has revealed opportunities for expanding its intelligence capabilities. In response to another recent audit, Customs' Report of Transportation of Currency or Monetary Instruments was revised to require the reporting of additional types of monetary instruments.

4. Narcotics Interdiction and Trade Enforcement

Despite years of concerted Federal effort, drug smuggling continues unabated. As an indicator of the magnitude of the illicit drug trade and challenges faced by Customs to stop it, the Office of National Drug Control Policy reported that over 1,120 tons of cocaine entered the United States during Fiscal Year (FY) 1999. For the same period, Customs reported that it had seized 172 tons of cocaine. Our prior audits have disclosed that Customs needs better narcotics examination criteria, better targeting systems, and more consistency in the performance and reporting of narcotics examinations.

In FY 2001, Customs expects to process 25 million entry summaries valued at $1.3 trillion, 503 million persons, and 149 million conveyances. However, the automated system Customs uses to process merchandise is outdated and unable to keep up with trade demands. The system also has significant control weaknesses. Customs recognizes that its ability to process the growing volume of imports, while improving compliance with trade laws, depends heavily on its modernization of the trade compliance process and supporting automated systems. The success of this effort is contingent on how well and how soon Customs is able to implement ACE.

5. Revenue Protection

Based on our work, we believe that stronger internal controls and system improvements would increase revenues collected by Customs and the Bureau of Alcohol, Tobacco and Firearms (ATF). For example, Customs recognizes its revenue collection rate is less than 100 percent and reported a revenue gap (the estimated net amount owed the government for non-compliant consumption entries) of $252 million for FY 1999. We believe Customs could significantly reduce uncollected revenue through its planned large-scale systems improvements discussed previously. Our recent audits of ATF have also identified control weaknesses over the tax-free status of tobacco and spirits exports.

6. Violent Crime

Despite a decline in the overall crime rate, violent crime remains a serious problem in the United States and remains the nation's number one public safety concern. Our recent audits of a major ATF program aimed at reducing violent crime, the Youth Crime Gun Interdiction Initiative (YCGII), found a number of opportunities for improvement. YCGII has the primary goals of tracing every recovered crime gun in participating cities through ATF's National Tracing Center and analyzing the resulting crime gun information to determine the community-wide patterns relating to recovered firearms. We found that ATF needed to do a better job of implementing the YCGII program and accounting for resources. Also, ATF needed to develop performance indicators that better measure YCGII's impact on reducing violent crime committed by youth. ATF agreed with our audit recommendations and is taking corrective actions.

7. Implementation of the Government Performance and Results Act

Integrating the Government Performance and Results Act's (GPRA) reporting requirements with traditional budget formulation and execution activities and the financial reporting requirements of the Chief Financial Officers Act of 1990 and the Government Management Reform Act of 1994 continues to serve as a worthwhile challenge for all Federal government agencies, including Treasury. Critical to this challenge are the collection, integration, and management of reliable performance data. To validate Treasury's data, we recently audited the accuracy and reliability of certain key performance measures. Through these audits we identified data errors and made recommendations for improving data reliability. While Treasury has improved the quality of the data stored in its automated and manual systems, we anticipate continued difficulty in the collection and management of reliable performance data.

Additionally, improved managerial cost accounting is necessary for the Department to effectively report and evaluate program performance. Accurate cost information is needed to identify the full costs of programs, activities, and outputs. The linkage of costs with performance measures is essential for informative reporting and meaningful cost/benefit analysis. The Department has initiated actions to improve managerial cost accounting; however, at most bureaus these efforts are still in the early stages.

Treasury has improved its strategic planning process and reassessed its strategic goals this past year. As a result of our assessment of Treasury's FY 1999 Performance Report and FY 2001 Performance Plan, Treasury modified the way it tracks performance goals and measures.

8. Financial Management at Treasury/Compliance with the Federal Financial Management Improvement Act

Treasury continues to face significant challenges to meet the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). FFMIA requires Federal agencies to implement and maintain financial management systems that comply substantially with Federal Financial Management System Requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. As reported in connection with our audit of Treasury's FY 2000 financial statements, Treasury is not in substantial compliance with the requirements of FFMIA.

Treasury, as well as individual component entities that were audited, received unqualified opinions on their FY 2000 financial statements. This is a notable accomplishment, however in certain cases it was achieved only through extensive efforts after year-end to overcome material weaknesses in internal controls to develop auditable financial information. Also, financial systems were not adequately integrated to support fiscal management of program delivery as well as budget execution functions and internal and external financial reporting requirements. These conditions precluded Treasury and a number of its bureaus the ability to generate timely and accurate information for routine operating and decision-making purposes, as well as for annual financial reporting.

9. Safety and Soundness of the Banking Industry

Clearly, a safe and sound banking system is a pre-condition for stability within our financial system. Through OCC and the Office of Thrift Supervision (OTS), Treasury regulates and supervises banks and thrifts with combined assets of over $4.2 trillion that account for over 58 percent of total industry assets. In addition, OCC-regulated national banks account for approximately $14.4 trillion of the off-balance-sheet assets, also known as financial derivatives. For nearly a decade the banking industry has experienced record profits, and bank failures continue to be minimal with less than 10 per year since 1995. However, recent signs of a slowing economy have become more evident given higher commodity prices and the spike in corporate bankruptcies. For the second quarter of Calendar Year 2000, the banking industry's earnings not only declined but also were the lowest since 1997.

Aside from fundamental economic factors, added regulatory and supervisory challenges arise out of the recently enacted Gramm-Leach-Bliley Financial Services Modernization Act (GLBA). This legislation lifted decade old restrictions on affiliations among banks, securities firms, and insurance companies. With it, additional supervisory challenges may also arise in other areas such as money laundering, the Community Reinvestment Act, financial privacy, predatory lending, and the expanded sharing of regulatory responsibility under the new law's functional regulation provisions. For example, we recently reported that the business of banking is evolving to include selling insurance, and this activity is expected to expand with the passage of GLBA. While insurance activities have traditionally been under the functional regulation of states, we believe that OCC needs to determine the reliance it can place on state supervision, and better define its supervisory role over national bank insurance activities.

Should you or your staff have questions, you may contact me at (202) 622-1090, or a member of your staff may contact Dennis Schindel, Assistant Inspector General for Audit, at (202) 927-5400.

FEDERAL STATUTES IMPACTING OIG AUDITS AND INVESTIGATIONS

Federal Managers' Financial Integrity Act of 1982, P.L. 97-255.

This act amended the Accounting and Auditing Act of 1950 and requires ongoing evaluations and reports on the adequacy of the systems of internal accounts and administrative controls of each executive agency.

Financial Institutions Reform, Recovery and Enforcement Act of 1989, P.L. 101-73.

FIRREA requires an annual audit of the Office of Thrift Supervision; Treasury OIG has been tasked with this work.

Chief Financial Officers Act of 1990, Pub. L. No. 101-576.

The CFO Act added to 31 U.S.C. § 3521 a requirement that each financial statement prepared by an agency in accordance with 31 U.S.C. § 3515 [see discussion of Government Management Reform Act of 1994, below] shall be audited in accordance with applicable generally accepted auditing standards by the Inspector General or by an independent external auditor, as determined by the agency Inspector General. A report on the audit is to be submitted to the head of the agency, and may be reviewed by the Comptroller General of the United States.

Federal Deposit Insurance Corporation Improvement Act of 1991, P.L. 102-242.

A provision of FDICIA, codified at 12 U.S.C. § 1831o(k), requires the OIG to conduct Material Loss Reviews (MLRs) in certain cases of failures of financial institutions regulated by the Comptroller of the Currency or the Office of Thrift Supervision which result in material losses to the deposit insurance fund.

United States Mint Reauthorization and Reform Act of 1992, P.L. 102-390.

This statute requires the Treasury IG to perform, or designate a public accounting firm to perform, an annual audit of the Mint. Subsection (e)(3) of 31 U.S.C. § 5134, which establishes the Numismatic Public Enterprise Fund, requires an audit of the annual financial statements of the Fund, to be done by the OIG or by an independent external auditor, as designated by the Secretary.

Treasury Forfeiture Fund Act of 1992, P.L. 102-393.

This statute established a fund within the Department of the Treasury to receive property forfeited by Treasury bureaus, and to make payments and awards associated with such forfeitures. Subsection (f) of the Act makes the Fund subject to annual financial audits under the CFO Act; Treasury OIG has been tasked with this work.

Government Performance and Results Act of 1993 (GMRA), Pub. L. No. 103-62.

This Act requires executive agency heads to submit to the Director of the Office of Management and Budget (OMB) and the Congress a strategic plan for performance goals of their agency's program activities. The plans cover at least a five-year period and must be updated at least every three years. They must be included in the President's budget.

Under GPRA agency heads must report annually to the President and the Congress on program performance for the previous fiscal year, setting forth performance indicators, actual program performance, and a comparison with plan goals for that fiscal year.

Government Management Reform Act of 1994, P.L. 103-356.

Section 405 of GMRA amended 31 U.S.C. § 3515 to require audited financial statements of certain government agencies, including the Department of the Treasury, and tasked the Office of Management and Budget to designate entities within departments that must have audited financial statements. Per OMB Bulletin 98-08, the Internal Revenue Service, Customs Service, and Bureau of Alcohol, Tobacco and Firearms are designated Treasury entities.

Federal Financial Management Improvement Act of 1996, P.L. 104-208.

FFMIA is intended to provide for consistency in agency accounting and to improve performance. The Act amended Section

5 of the Inspector General Act, 5 U.S.C. Appendix, to requires Inspectors General to report to Congress instances when their agencies have not met targets in making their accounting systems compliant with the requirements of the Act.

Information Technology Management Reform Act of 1996 (Clinger-Cohen Act) (Federal Acquisition Reform Act of 1996), P.L. 104-106.

Under this act, the OIG performed an audit to determine the progress of the Department of the Treasury to manage, evaluate, and make strategic decisions about Treasury's portfolio of information technology initiatives.

The Act mandated that departments establish processes and provide information to help ensure that IT projects are being implemented at acceptable costs, and within reasonable and expected time frames. It also required IT management processes to be institutionalized throughout the organization and used for all IT related decisions.

National Capital Revitalization and Self-Government Improvement Act of 1997, Pub. L. No. 105-33.

Under this Act, the Secretary of the Treasury is responsible for the selection and oversight of the Trustee of the District of Columbia Federal Pension Liability Trust Fund. This statute requires an annual audit of the fund; Treasury OIG has been tasked with this work.

Internal Revenue Service Restructuring and Reform Act of 1998, P.L. 105-206.

Section 1103(d) of the RRA specifically tasks the Treasury OIG with performing audits of the financial statements of Treasury

Government Information Security Reform Act, P.L. 106-398.

This act, Subtitle G of the Defense Appropriations Act, is intended to ensure the effectiveness of controls over the information resources that support government operations. It requires processes to coordinate information security oversight, and assigns to agency heads responsibility to ensure the integrity and confidentiality of information systems, and to develop information security policies, procedures and controls. It requires risk assessments and annual independent evaluations of security programs, and assigns to agency Inspectors General responsibility for assessing agency compliance with the Act's requirements by performing the required evaluations.

<u>Reports Consolidation Act of 2000</u>, P.L. 106-531.

This act authorizes consolidation of financial and performance management reports made pursuant to, <u>inter alia.</u>, 31 U.S.C. § 3515 and 3521. It specifically requires agency Inspectors General to report their views on the "most serious management and performance challenges facing the agency," and their assessment of the agency's progress in addressing those challenges. These IG statements are to be forwarded via the agency head, who can provide comment on them before transmitting them to Congress.