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NOMINATION OF ERIC THORSON TO BE INSPECTOR GENERAL OF THE SMALL BUSINESS ADMINISTRATION

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP UNITED STATES SENATE

ONE HUNDRED NINTH CONGRESS

SECOND SESSION

MARCH 1, 2006

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NOMINATION OF ERIC THORSON TO BE INSPECTOR GENERAL OF THE SMALL BUSINESS ADMINISTRATION

WEDNESDAY, MARCH 1, 2006

UNITED STATES SENATE,
COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP,
Washington, D.C.

The Committee met, pursuant to notice, at 2:07 p.m., in room SR–428, Russell Senate Office Building, the Honorable Olympia J. Snowe (Chair of the Committee) presiding.

Present: Senators Snowe, Isakson, Vitter, Kerry, Landrieu, Bayh, Pryor, and Grassley.

OPENING STATEMENT OF THE HONORABLE OLYMPIA J. SNOWE, CHAIR, SENATE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP, AND A UNITED STATES SENATOR FROM MAINE

Chair SNOWE. The hearing will come to order. Good afternoon and welcome to today's hearing to consider the President's nomination of Mr. Eric Thorson to be the next Inspector General for the Small Business Administration. I also want to welcome the Ranking Member of this Committee, Senator Kerry, and thank him for working with me on this nomination and this hearing as well.

I also appreciate my colleague, Senator Grassley, for his presence here. Senator Grassley will be introducing Mr. Thorson, who previously served as Chief Investigator for the Senate Finance Committee.

We come to this hearing at a time when the Inspector General's role at the SBA will be all the more critical given the enormous challenges the Agency has faced, and continues to confront, areas such as the disaster loan program's operation and the unacceptable response to Katrina and Rita, enforcement of government-wide small business contracting rules, and the oversight of SBA lending problems.

Therefore, it is imperative that the new Inspector General be aggressive and tireless as the unprecedented challenges require unprecedented responses. So Mr. Thorson, I look forward to hearing your testimony to further explore your qualifications to carry out as the Inspector General at this pivotal juncture for America's 25 million small businesses and their employees.

Mr. Thorson certainly brings a depth and breadth of experience from having served, among other roles, as Director of Defense

Issues for the Legislation and National Security Subcommittee of the House Government Operations Subcommittee, Chief Investigator for the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs, and for the Senate Committee on Finance, and Special Assistant to Senate Republican leader Trent Lott on corporate fraud investigations.

His past investigative subjects include such major issues as Enron and WorldCom. And he worked in both the executive and legislative branches under Republicans and Democrats, including Representative John Dingle and Representative John Conyers, and the late Senator Bill Roth as Chairman of the Finance Committee at that time, and, as I mentioned, the then-Majority Leader Trent Lott, during his many years of investigative experience. Moreover, he has had firsthand knowledge of the trials, challenges, and gratification of being a small business owner who fulfilled his dream with the help of an SBA veteran's loan.

Indeed, we have an obligation to ensure that the person confirmed as the SBA Inspector General is not only a well-qualified investigator. They must also show passion in identifying barriers that may limit the success and entrepreneurial spirit of our small businesses, that form the very foundation of the Nation's economic growth and job creation potential, having created about three-quarters of all net new jobs annually.

In that light, the Inspector General's office recently began an investigation of the SBA's woeful response to Hurricanes Katrina and Rita, an area that I and Senator Kerry and this Committee has investigated at length. As we have learned, the Agency's Disaster Credit Management System was incapable of handling the high volume of disaster loan applications—nearly 350,000 have been received so far—and the SBA failed to accurately monitor its disaster financial information and to implement its disaster transformation workforce strategy. This tragic response to a tragic and devastating disaster must not be repeated. The Inspector General will be key in determining how we can ensure such bureaucratic lethargy never reoccurs at the SBA.

Mr. Thorson, you will also bear the responsibility of determining, whether SBA's administrative procedures measure up to the expectations of America's small business owners. We've seen what cannot happen under the Inspector General's watch with the STAR loan program, epitomized by the Inspector General's December 2005 report finding that eligibility could still not be determined for 85 percent of the loans reviewed.

The series of ongoing investigations on the effectiveness of the SBA's Lender Monitoring System, which is used to provide oversight of lenders and of SBA's handling of lending programs such as the 7(a) and 504 business loans, further underscores the Inspector General's vital part in providing aggressive oversight and minimizing abuses of the system.

Similarly, given recent discoveries of small businesses losing prime contracting opportunities to large businesses due to poor oversight of contracting laws, it is fitting that you will bring to this appointment 12 years of experience in successfully investigating and reforming Federal contracting programs. Uncovering, monitoring, and correcting abuses, lax implementation of laws, or waste,

fraud, and abuse of taxpayers' funds, will require your urgent attention, Mr. Thorson. With your success, it will be America's small businesses that reap the greatest reward.

Finally, let me say that, obviously, this hearing has been delayed to provide additional time to thoroughly examine documents pertaining to the 1997 and 1998 hearings on the Internal Revenue Service abuses held by the Finance Committee under the leadership, at that time, of Chairman Roth, where Mr. Thorson was Chief Investigator.

During this additional time period, we've had further opportunity to analyze all of the issues, documents, and talk to people involved in those investigations as well. As the record would ultimately show, these hearings led to the enactment of the Internal Revenue Service Restructuring and Reform Act that we passed, 96 to 2, by the way, in 1998.

Mr. Thorson, I welcome you. I also want to welcome your family. I know your wife Susan is here today. Would you like to introduce other members of your family at this point in time, and then we'll move on to Senator Kerry.

Mr. THORSON. Thank you. My wife, Susan, and her father, Arthur White. My sister, Karen Miller, with her husband, Jim, and my nephew, Chris Miller.

Chair SNOWE. Well, we welcome all of you here today. Thank you for being here with us.

Now I'd like to recognize Senator Kerry.

OPENING STATEMENT OF THE HONORABLE JOHN F. KERRY, A UNITED STATES SENATOR FROM MASSACHUSETTS

Senator KERRY. Thank you very much, Madam Chairman. I personally appreciate your efforts. Thank you for allowing the Committee to conduct the necessary due diligence on this nomination.

Mr. Thorson, welcome, and welcome to the members of your family also. Of course, we welcome Senator Grassley, for whom both you and I have enormous respect. I think his introduction is important to all of us here. Let me just say that I also want to thank Senators Levin and Lieberman and their staffs for their work in reviewing this nomination, which they also requested to do.

You know, it's not often that this Committee is charged with confirming administration nominees. But regardless of the infrequency of the activity, and given the potential impact that these nominees could have on an already fragile Small Business Administration, this is a duty that we do take seriously.

The need for the SBA Inspector General to be impartial and free of political influence from either side, to be someone who will act in the best interest of the Agency, and most importantly, in the best interest of small businesses and citizens across the country, and the taxpayers whose dollars are being spent, that's really an importance that can't be overstated here.

We rely heavily on the work of the SBA's Inspector General for unvarnished investigations and analysis. In 2005 alone, the SBA Inspector General's office released reports critical of the administration's enforcement of anti-bundling rules, reductions in staff, and enforcement of small business contracting laws.

There's much more oversight to be done, as we discussed Mr. Thorson, work that will require an independent IG who's willing to conduct thorough investigations to address the serious management problems afflicting the Agency.

These issues include: Large businesses receiving contracts intended for small businesses, and being counted as small businesses when they're not; a review of the challenges facing the mentor/protege program; an audit of the contract bundling review process and the inadequate staffing level of PCRs that led to 87 percent of bundled contracts not being reviewed; major staffing shortfalls in the staffing at the Office of Technology that oversees the SBIR and SDTR programs; inadequate staffing and shortfalls in oversight of the 504 liquidation program; and most urgent, the continued inadequate response to victims of Hurricanes Katrina and Rita by the SBA Disaster Loan Program, and the continued shortfalls in SBA oversight of contracts being awarded to rebuild the hurricane-affected region.

Now, Madam Chairwoman, I know you know, and I know you believe this as I do: The IG does not belong to a party. It's appointed by a party. It's appointed by a President. But it really assumes a very special trust. There are pressures. We all understand the pressures of politics. But this trust is most important.

Now, unfortunately, this nomination comes at a time where there's a growing concern over the numbers of Inspectors General who are put into that position with very specific political ties to an administration that simply doesn't have a strong record of nominating people who are going to really be free and independent.

In January of last year, Representative Waxman, who's the Ranking Member of the House Committee on Government Reform, released a report stating that over 60 percent of the IGs appointed by the Bush administration have had prior partisan political experience, while less than 20 percent have had audit experience, which is what they're really being nominated for.

Now, after reviewing Mr. Thorson's background, it's clear that unlike many of the IG nominees discussed in the Waxman report, he does have extensive investigative experience. I welcome that. I mentioned that in our conversation.

The issue has really been one that has arisen about the willingness in the record to address serious management challenges within the agencies. Will you be an IG who can conduct investigations in a nonpartisan manner and who will work diligently to identify the larger programs within the agency?

Now, Madam Chair, as you know, in reviewing the record, questions were raised by outside entities that came to the Committee with respect to the taxpayer abuse hearings of the Finance Committee that were held in 1997 and 1998, of which Mr. Thorson was the lead investigator.

There were two GAO reports that concluded—it's their conclusion, not mine, not this Committee's, but their conclusion with which we needed to obviously review the record—that almost all of the claims made during the hearings were either unfounded or inaccurate, and from reports at the time and in subsequent interviews we have heard that they were, in fact, highly partisan hearings.

Now, I know Mr. Thorson, in our conversation, you dispute that, and you will have your chance on the record to make your statements about it. I have said that I don't intend to oppose this nomination, and I don't. I think it is important for the record to adequately reflect what happened in the course of that. Our much-respected colleague, now deceased, on May 4, 1998 in the New York Times, Senator Daniel Patrick Moynihan, who both served as Chair and Ranking Member, I believe, said the hearings were "one-sided and partisan." That was his judgment as a senior Senator and Member of that Committee.

You had complete authority over those investigations and were the only staff person responsible for clearing the witnesses prior to those hearings. The key here is not to go back and relitigate. The key here is to have confidence that as we go forward, this Committee will have confidence, real confidence, that if we put you in this position, that we can expect accountability within the Small Business Administration, and accountability that's based obviously on fairness and on a completely nonpartisan record.

We need a strong IG who will conduct those kinds of investigations. It serves all of us—the Committee, the Congress, the Administration—to have that. I look forward to your testimony and to some answers to questions as we proceed.

Thank you, Madam Chairman.

Chair SNOWE. Thank you, Senator Kerry.

Senator Vitter, do you care to make any comments?

Senator VITTER. No.

Chair SNOWE. Senator Pryor.

Senator PRYOR. No.

Chair SNOWE. Thank you.

Here today to introduce Eric Thorson is our colleague, Senator Grassley. Senator Grassley is Chair of the Finance Committee. We certainly welcome you to this Committee here today.

Chairman Grassley has had an extensive working relationship with Mr. Thorson as far back as 1993, where he served as lead defense investigator for the House Committee on Government Operations, as well, of course, on the Senate Finance Committee.

Senator Grassley, thank you for joining us here today. Your full written statement will be entered in the record, and we look forward to hearing your introduction of Mr. Thorson.

OPENING STATEMENT OF THE HONORABLE CHARLES GRASSLEY, A UNITED STATES SENATOR FROM IOWA

Senator GRASSLEY. Madam Chairwoman and Senator Kerry, it's an honor for me to come before the Committee to introduce Mr. Thorson. I would associate myself with the remarks of Senator Kerry about the necessity for the independence of the Office of Inspector General, the importance of the office.

In addition to saying that I come to support Mr. Thorson and agreeing with Senator Kerry about the independence of the office, even in this administration, I'm going to take credit for, although some people say maybe I shouldn't take credit for, the removal of at least three Inspectors General who I felt were not doing their job. Maybe somebody would even add it up to more. I pay a great deal of attention in both Republican and Democratic administra-

tions to make sure that Inspectors General are independent, as Senator Kerry has said.

As both of you know, I've worked very hard to strengthen the oversight role of Inspectors General throughout the Government. The IGs are our first line of defense against fraud, waste, and abuse in Government. We depend on them to ensure that every tax dollar spent is spent according to law. When that doesn't happen, we in Congress need to know about it and take corrective action.

As you also know so well, being an IG is a tough job, and particularly when they're independent, as Senator Kerry says. When the IGs aren't doing their job, we need to know that they're not doing their job. Congress also has a responsibility to watch the watchdogs. We in Congress need to keep a sharp eye on the IGs to make sure that they're meeting their responsibilities under the IG Act.

What I'm saying, Madam Chairwoman, is this: It takes a very special person to be a good IG. Above all else, an IG must have integrity and courage. IGs must be independent. They must always set an example of excellence in their personal conduct. IGs must meet high standards indeed.

To the two leaders of this Committee, I say Mr. Thorson meets those standards. Mr. Thorson has an outstanding reputation for being a man of integrity and courage. He has the requisite knowledge, experience, and character to be an IG in the Small Business Administration.

He has senior-level management experience in government, having served as Assistant and Deputy Assistant Secretary of the Air Force 1985 to 1989. He has executive-level experience in the private sector as well, where he was president of his own company that operated a fleet of corporate jet aircraft.

His investigative credentials I think are impressive. Some of these were referred to already, but let me repeat: 1997 to 1998, Chief Investigator, Senate Finance Committee. He led the investigation of the abuses of the Internal Revenue Service. His findings and recommendations formed the foundation for an excellent set of hearings. Those revelations that did surface at those hearings helped to generate national support for the reform and companion legislation that followed for the IRS.

1995 to 1997, Mr. Thorson was Chief Investigator of the Senate Permanent Subcommittee on Investigations. Prior to that, in 1995, he served as the Lead Defense Investigator for the House Committee on Governmental Operations.

During the timeframe, 1993 to 1997, I became directly involved in at least three of Mr. Thorson's investigations and testified at hearings on those matters. At the time, I remember being so impressed with the very professional way Mr. Thorson conducted investigations, especially an investigation involving the Air Force C–17 contract.

On the C–17 investigation, he worked in close concert with the Defense Department IG. That kind of cooperation was in keeping with the true spirit of the IG Act, and Mr. Thorson is the one who made that happen. On March 17, 1993, the IG presented a devastating report to the House Committee on the back-door bailout of the C–17 contract.

I was there. I remember it well. I was a witness and testified at that hearing. After complimenting the Chairman, Mr. Thorson, and the IG for working together to produce a superb piece of work, the record shows that I then said this: "This is oversight and investigation at its best." These words were meant for you, Mr. Thorson.

Chairwoman Snowe, I know that Mr. Thorson is capable of doing, and I feel confident that he can do, what IGs are supposed to do and do it very well. In my book, he has passed the IG test with flying colors. I'm confident of Mr. Thorson's ability to be impartial and independent, to be objective and thorough.

Above all, and in closing, I would mention things that have been referred to here and simply say: "Take all of the work of Inspectors General and people that are whistleblowers and everything else of people trying to cut out things that are wrong in Government." I know that there have been some tough questions asked. On that score, I would say that my own experience has taught me that the hard-hitting investigations always generate friction and generate criticism. Always. It goes with the territory. It's a fact of life in that line of work.

I came here this afternoon to stand before you with Mr. Thorson because I believe he has what it takes to be that top-notch IG that both of you have defined. If I could, just for another Senator, an e-mail between Senator Kyl's office and my office says something like this—I don't like to put e-mails in the record, but I'll save it for you so you can prove that I said it—Kyl's office just asked—CEG mentioned that Kyl also supports Mr. Thorson.

Thank you.

Chair SNOWE. That will be included without objection.

[The information follows:]

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February 27, 2006

The Honorable Olympia Snowe
Chair
Committee on Small Business and Entrepreneurship
428A Russell Senate Office Building
Washington, DC 20510

Dear Senator Snowe:

It is my understanding that you are considering the President's nomination of Eric Thorson for the position of Inspector General at the Small Business Administration (SBA).

Eric served in a variety of capacities in the United States Senate, most recently as a Special Assistant to Senator Trent Lott during his tenure as Majority Leader. He also served as the Chief Investigator for the Senate Finance Committee and the Permanent Subcommittee on Investigations. During his time working in the Senate, I had the opportunity to interact with him personally, and I can attest to his abilities and integrity. I believe he possesses the skills and background to be an effective Inspector General at the SBA, and I recommend him highly for the position.

Thank you for your consideration.

Sincerely,

JON KYL
United States Senator

JK:DA

Chair SNOWE. Thank you, Chairman Grassley, for being here today. Thank you very much.

Senator GRASSLEY. Thank you.

Chair SNOWE. Appreciate it.

Senator Landrieu, do you care to make any comments before we begin?

Senator LANDRIEU. No.

Chair SNOWE. Okay. Mr. Thorson, Rule 3 of the Committee requires that all witnesses at nomination hearings give their testimony under oath. If you would please stand and raise your right hand so the oath can be administered. Do you swear that the testimony that you are about to give to this Committee will be the truth, the whole truth, and nothing but the truth?

Mr. THORSON. I do.

Chair SNOWE. You may be seated. And you may begin.

STATEMENT OF ERIC THORSON, NOMINEE FOR INSPECTOR GENERAL OF THE SMALL BUSINESS ADMINISTRATION

Mr. THORSON. Good afternoon, Senator Snowe and Senator Kerry. It is a privilege to come before you for consideration to be the next Inspector General of the Small Business Administration, and I thank you for allowing me to make a brief opening statement.

I hope that in reviewing my qualifications for this nomination, you will find that I bring a strong, varied background of related Government experience to this position. I have served in the military as an Air Force pilot, in several executive branch agencies, and as an investigator for a number of Committees in both the House and Senate.

I began my Government service as a cadet at the U.S. Air Force Academy. By that time in my life, I had lost both my parents and I could not even pay the uniform deposit required upon entrance. I have always looked upon this opportunity as a true gift that forever changed my life and set the foundation for a debt to this country that I will never be able to repay no matter how many years of Government service I accumulate.

After spending 2 years flying in Southeast Asia, I left the Air Force in 1973. I started a tiny flight school in southern California with 3 single-engine airplanes. The capitalization of the company came from my only credit card. I learned that there was a Government agency that had a unique program to assist Vietnam returnees with loans to develop a business. I applied.

One day, I received a call from the Small Business Administration that I had been approved for one of these special loans. I was stunned. By 1985, I had paid back the SBA loan in full, and my company was operating over 20 private jet aircraft, primarily for the movie industry. My clients included Frank Sinatra, Clint Eastwood, Merv Griffin, and Henry Fonda. This most interesting time in my career would not have been possible except for the SBA.

1985 was also the year that I was offered a position by the Reagan administration as Deputy Assistant Secretary of the Air Force for Economic Analysis and Financial Controls. Given my background with the Air Force, that was not something I could turn down. It was time to start paying back.

I mentioned earlier having been a congressional investigator. In 1995, I had the privilege of being named the Chief Investigator for the Senate Permanent Subcommittee on Investigations, one of the most incredible jobs I have ever had.

Part of that enjoyment came from working for a very fine man, the late Senator William Roth. He believed in the importance of nonpartisan oversight and demanded an exceptionally high degree of accuracy and integrity in the investigations that he authorized. Those lessons are particularly applicable to any Inspector General. During that time, we conducted investigations involving defense contractor fraud, Medicare fraud, and even the Russian Mafia.

Today, as the nominee to be an Inspector General for the SBA, we are on the edge of what I believe will be a crucial test for the Agency. As a result of Hurricanes Katrina and Rita, the SBA is at the forefront for the disaster relief loans, which will involve unprecedented numbers, both in applications and dollars.

Also, history has proven that in this kind of situation, we can expect there to be an unprecedented number of attempts to defraud the program. It is strongly stated that the first goal of the office of the Inspector General is to "Prevent fraud and unnecessary losses in SBA programs." The word "prevent" clearly implies the need to be proactive, to stop fraud before it can be accomplished, and to create a deterrent to those who might be planning on taking advantage of this Nation's efforts to assist those who have lost so much.

If confirmed as the Inspector General, I can assure you that the entire office, both auditors and investigators, will use every means to deter such efforts, and work with the administrator of the SBA in finding ways to ensure these vital loans are distributed to only those in true need.

I sincerely hope that you find my background and experience worthy of this position, and I look forward to answering any questions you might have.

[The prepared statement of Mr. Thorson follows:]

Statement

of

Eric M. Thorson

Before the

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP

March 1, 2006

Good morning, Sen. Snowe and members of the committee. It is a privilege to come before you for consideration to be the next Inspector General of the Small Business Administration. Thank you for allowing me to make a brief opening statement, and I hope that in reviewing my qualifications for nomination, you will find that I bring a strong, varied background of related government experience to this position. I have served in the military as an Air Force pilot, in several executive branch agencies, and as an investigator for a number of committees in both the House and the Senate.

I began my government service as a cadet at the U.S. Air Force Academy. By that time in my life I had lost both my parents and could not even pay the uniform deposit required upon entrance. I have always looked upon this opportunity as a true gift that forever changed my life, and set the foundation for a debt to this country that I will never be able to repay no matter how many years of government service I accumulate.

After spending 2 years flying in Southeast Asia, I left the Air Force in 1973. I started a tiny flight school in Southern California with 3 single engine airplanes. The capitalization of the company came from my only credit card. I learned that there was a government agency that had a unique program to assist Viet Nam returnees with loans to develop a business. I applied. One day, I received a call from the Small Business Administration that I had been approved for one of these special loans. I was stunned! By 1985, I had paid back the SBA loan in full, and my company was operating over 20 private jet aircraft, primarily for the movie industry. My clients included Frank Sinatra, Clint Eastwood, Merv Griffin and Henry Fonda. This most interesting time in my career would not have been possible except for the SBA.

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General is to, "Prevent fraud and unnecessary losses in SBA programs." The word "prevent" clearly implies the need to be proactive, to stop fraud before it can be accomplished, and to create a deterrent to those who might be planning on taking advantage of this nation's efforts to assist those who have lost so much. If confirmed as the IG, I can assure you that the entire office, both auditors and investigators, will use every means to deter such efforts, and to work with the Administrator of the SBA in finding ways to ensure these vital loans are distributed to only those in true need.

I sincerely hope that you find my background and experience worthy of the position of Inspector General. I look forward to answering any questions that you might have for me.

Chair SNOWE. Thank you, Mr. Thorson. We appreciate that.

I'd like to begin with your experiences as the Chief Investigator of the Senate Finance Committee because obviously Senator Kerry has raised some of those issues here today. I'd like to have you provide some insight into your experiences and how you approached that investigation because I think it would be helpful as well to the Committee. As I said earlier, we've talked to a number of people who—in fact, many of whom spoke very highly of you throughout the process in working with you and the number of positions that you've held, both on the House and Senate Committees.

In response to the Committee, you highlight, obviously, your experience. As you're aware, and what Senator Kerry raised about the follow-up to the review of the Government Accountability Office's report, that they were not able to substantiate many of the claims that were made by witnesses during the course of the IRS hearing.

I know that former Chairman Roth wrote in his book about the hearings, "The Power to Destroy," that, "Our investigators and professional staff members on the Finance Committee made certain that the evidence being gathered was corroborated by two or three witnesses and vetted against taxpayer files."

I'd like to have you lay out for the Committee: What were your criteria for selecting and vetting witnesses?

Mr. THORSON. First of all, we used different criteria for different types of witnesses. The first thing that Senator Roth originally started to do here was to look at abuses, which means taxpayer cases. We started receiving them, first a trickle, then hundreds, and eventually thousands.

In that mail, we began to get letters from IRS employees who basically said, "If you're serious about trying to help this agency, we'll help you." I didn't pay much attention to those. I admit that. That wasn't what we were doing. We were looking at taxpayer cases. More and more, I began to look at some of these letters and realized eventually that if we were going to tell this story, it had to be told by the people who really worked there and who lived in those jobs.

For the taxpayer cases, specifically on the taxpayer abuses, I believe there was one panel. We're going back a ways, but there were some criminal division cases. But the regular taxpayer cases, what we did there, we had 6103 authority granted by the chairman, and we went back and we took their stories. We had many, many that we could have chosen from. The stories really were heart-rending. I mean, they were terrible.

We decided, first of all, these should be people that owed no tax, in our best estimation. We knew that no matter how bad the story were, when we put these hearings on, if these people—there would be somebody on the panel who would say, "well, if they'd just paid their taxes, they wouldn't have had this problem." We eliminated that by picking only cases where we believed these people did not owe anything.

Once we had that narrowed down, we then went back to the IRS and pulled their files. By the way, this is also intending to show that they knew who we were talking to. It wasn't like they didn't know because we had to go to them to get the files.

We recovered their files, and went and looked to see that what they were telling us matched what the IRS was telling us. Obviously, in the cases that we did put on, that was clearly the case. We knew everything the IRS knew about them. That's how we chose those taxpayers.

Those cases were also to represent more than just a story. They were supposed to represent things that we had heard numerous times, not just a one-time situation. You can always find those. The idea was that some of these stories would really resonate, and that they—that we heard it here, here, and here, and we chose a witness to exemplify that.

I will tell you that one of the stories we heard involved a husband and wife having to divorce in order to protect her second husband's paycheck. He had nothing to do with the tax year for which he was—the woman here was being—the money was being taken from them. They went after her second husband. They ended up having to divorce.

What I found was, that wasn't unusual, that that advice was being given by tax counsel in order to protect income. Now, that should never happen. That never, ever should—people should never have to get a divorce because of their government. So we chose that particular case.

By the way, I want to tell you, forgive me. I do get passionate about this, so forgive me about this. I lived this for 2 years.

When we chose this particular woman and we asked her if she would tell her story, she said that it was so important, given what her family had been through, that her whole family would be at the hearing. We said, "ma'am, we can't do that. We have rules about what we can pay, and we can pay your travel but we can't do that."

And she said, "Oh, no, that's okay. That's not what I mean." And I said, "Well, what are you getting at?" Because logistics was a huge part of these hearings. What it boils down to, and I don't mean to drag this out, but it's something I'll never forget, it was so important that the United States Senate would deal with this issue that affected her life, she and her husband, and her kids, got in their car and they drove here from San Diego, California.

That's the kind of thing that drove this. Senator Kerry, I appreciate very much the time you spent with me yesterday. We talked about this kind of thing. I tried to assure you then, and I will assure you now, there were no politics to this. I have no idea what party any of these people belonged to—I didn't care who owned the IRS at that time, or anything else. Those were the kinds of things that we were dealing with.

To get back to the issue, not trying to drag this out too much, but the idea was with taxpayers, A, they owed no tax. And B, their story matched what was within the IRS files.

When it came to employees, we realized first of all that there was one thing I'd never run into before, ever, and that was Federal employees who feared their own agency. It was almost universal. Even people who had never had a problem within their agency, they knew the kind of things that could happen to them. I have a number of quotes that I won't read unless I'm asked specifically, but with people of 25 and 30 years' experience that went into this

sort of thing. We knew we had to try and figure out how we were going to present this.

What we decided was, among ourselves—so nobody set this for us; we did this ourselves—first of all, we wanted every division that we could get represented. That's auditors, Examinations Division, and collections. We had heard about a group called inspections. That's internal affairs, and they carry weapons. District counsel. Maybe we could get their own lawyers. That's what we wanted to do. We wanted to spread it.

We also spread it geographically. We wanted to make sure that we drew our witnesses from every part of the country so we couldn't be accused of finding only some small pocket of problems.

The third that we set for ourselves, was the most difficult: 20 years with the IRS before you could be one of those witnesses. Now, this was the panel that we put on that was behind a screen. These people were scared. They asked for anonymity, and they asked that it not just be granted for the hearing but forever. They gave us some pretty good reasons why.

There is one person behind that screen who has gone public today because he's left the IRS. He was an inspections officer. He's now with the IG at Customs, and has been willing to talk to you all if you ever want to talk to him. He's a very fine person. Ironically, I probably have more friends in the IRS than anybody you'll ever meet.

That's kind of how we did that. How we verified some of the things that these people were saying was, first of all, one of the most difficult tasks of a congressional audit, because we don't have a badge, is to keep expanding your sources. One thing we were accused of was making cold calls to IRS people. We never, ever did that. They had to call us.

We had to expand that circle of sources and to make sure it spread out into different parts of the country. When a person would tell us that one thing existed, we would call sources in another part of the country and make sure, "Have you heard the same thing? Does this sort of thing go on?"

A perfect example of that was the fact that in auditors, for example, that audit taxpayers, not corporations, but small businesses and taxpayers, was: "We target poor people." I could never understand that because that doesn't make any sense. There's no money there.

They said, "No, you don't understand. This has nothing to do with money. This has to do with statistics." Open and close cases as fast as you can. When people are represented by counsel or they're represented by CPAs, it slows us down. We go after people who can't afford to have help.

That was universal. We heard that in every part of the country. We also heard the allegations of quotas. In one case, it was $1,000 an hour. In another case, it was $1,200 an hour. We asked for proof of that. We got it, in writing, where it was actually specified, $1,200 an hour. If I'm an auditor and I sit in your living room and I audit you, I'm going to bump your taxes by $1,200 an hour whether you deserve it or not. We heard that across the country. We found people who would be saying that. They would have their

own stories, but they would also corroborate them by saying the same thing.

The GAO report, for instance, references the situation of large corporations, where auditors of international, multi-national companies would zero out large tax debts. Now, first of all, they say there was no corroboration. Yet within their own report, they say four auditors from different parts of the country that didn't know each other, all testifying under oath, all said the same thing.

That is a form of corroboration. Maybe it doesn't meet somebody's standard. How could these four people—and remember, these aren't disgruntled taxpayers. These are people with 25 and 30 years with the IRS. These people know what goes on inside their agency, and they testified and came forward. None of these people were behind a screen. That's what they said.

Each witness was chosen to tell their own story, but also have an overlapping testimony where they testified as to something some of the other people said as well.

Senator Kerry, you made a number of points in your opening statement, and I appreciate them, and especially I will come back to the nonpartisan part because that's something we talked about that's very important to me.

The other part here is that when the GAO says, "we did not corroborate, we did not find, we did not verify, you've got to wonder," what were they doing? First of all, if I'm the one who, as they state here, that did the verification, how come nobody talked to me? How come nobody called and asked for an appointment to just see what I did? Nobody called my partner, either, who by the way is here in this hearing room today.

Why didn't that happen? I know of one witness they did interview, and she immediately filed a complaint with the Finance Committee and called me, even though I was out of Government at that point, and registered a complaint of bias by the interviewer.

In the case where we're talking about those kinds of things, where they talk about lowering tax debt because of influence, because of influences by a corporate taxpayer or whatever, one of the things the GAO did find was that, No. 1, if you read the reports—and again, I've got it specified; we don't need to go into it, but I can—those reductions did happen. They were correct on that. What the GAO says was they were within the discretion of the manager. But that was never an issue. That wasn't the point. The point was, why did they do that? And the allegation was influence.

Well, for example, one of these women who was an auditor, again, of multi-national companies—I can't even imagine trying to do audits of that kind—she made an allegation that one of her bosses maintained a law office on the side from the company who they were auditing, in Manhattan. I'm assuming the Manhattan corporate real estate is about the most expensive in the world.

Now, the GAO said, "Yes, we found that was true, but that was okay because we verified that their ethics person approved this." That was all right. That had nothing to do with it. The point was, they were operating a law office on the side in the facility belonging to the company that they were auditing.

Those are the kinds of things where I disagree strongly with the findings of the GAO. I think there were better ways that they could

have gone about this, and certainly by talking to me. I would have been very willing to. I'm hoping I've addressed most of the issues that may have come out of that.

Chair SNOWE. I appreciate that, Mr. Thorson. I think that's helpful to the Committee in offering your insights, and being able to personally do that here today. I noted in the late Chairman Roth's book on "The Power to Destroy" that he said that first and foremost, he wanted to ensure the investigation was fair, above and beyond everything else. I appreciate that. I appreciate your comments.

Let me move on to one of the small business issues, and then I'll move on to Senator Kerry. In this role of Inspector General that's so crucial and vital at this point, particularly in the history of Small Business Administration as far as I'm concerned, is the ability to deliver these programs and services in an efficient and effective way. As you know, the hurricanes, both Katrina and Rita, the Small Business Administration really had the opportunity to step up to the plate and to offer these programs.

Unfortunately, we had some considerable difficulties across the board—they were widespread from the outset—in administering these programs efficiently and effectively and expeditiously. There was virtually no anticipation in terms of the numbers of applications that would be filed and how to process them acquiring auditors and verifiers and so on and so forth.

How would you approach, for example, the particular problems that certainly manifested itself as SBA was responding to these hurricanes this last fall? They received more than 337,000 applications for disaster loans, they've approved 71,265, and they still have 105,803 applications pending. Obviously, what we have seen, what we have experienced, is the lack of urgency, the lack of speed and efficiency to the response, and it has been very slow in disbursing the funds. In fact, out of the 5.1 billion in loans, it's actually disbursed only 432 million to borrowers.

Obviously, without this money, as Senator Landrieu can attest, it's very difficult to rebuild and restructure the economy in New Orleans and throughout the Gulf region that's been hard-hit. How would you approach this particular investigation so that we can best learn from these mistakes and to prevent them, and anticipate them in the future?

Once it's obvious that a disaster is about to occur and it's imminent, that certainly the Small Business Administration should have positioned itself to begin to plan, as the Coast Guard anticipated, for example, in prepositioning its assets. Clearly, the Small Business Administration had an opportunity to begin to plan for how they were going to administer these disaster loans.

Mr. THORSON. Katrina and Rita I think created a situation that, while it's been said many times, nobody could anticipate. Maybe that's true to some degree. The truth is, once this started to happen, I think one of the things I was very surprised at was, to this day, there is not an IG presence by the SBA in the Gulf area. To be quite honest, I don't understand that. I think that's one of the things that has to happen immediately. That means from me on down. That is something I would intend to do immediately.

I think another thing is that you've got to put together basically—and this has been tried by, I think, Homeland Security before—is teams of people, both investigators and auditors. You need to go down and you need to see what systems are working and what systems are broken. I think Senator Kerry used the term "unvarnished" at one point, and that's exactly what it's got to be. You don't care who's offended by it, but you've got to figure out what is going on and where are the weaknesses.

Now, the IG doesn't set the policies, obviously, as to who gets a loan or who doesn't. You all do that with the Administrator. When those policies are established, the IG does measure what is happening against those policies, and then it reports to you all and it reports back to the Administrator as well. I don't see that happening right now.

Maybe—I don't mean to be unfair to the Agency. I've watched this and had some time to look at this, and I think that's one of the first things that has to happen.

Fraud has got to be a huge problem, given the amount of money that's flowing down there right now.

The second problem, and I would probably rank this right up there with it, is the small business set-aside issue that you've both raised in your correspondence. I've read all your correspondence. The contracting that's going to take place, both of what is happening right now and in the future, is just staggering.

I mean, the kind of things that will be contracted out to major corporations, we know that. You know that's going to happen. Then we have to take and set the policy, check the policies, and see what it is that the small businesses are entitled to, and then make sure that that's adhered to. It doesn't matter who you upset by doing that.

That's one thing—and again, Senator Kerry, I made you a promise. I made you a couple of promises. One was there would be no politics to what I do in this office. I want to state that publicly here on the record to repeat that because that's the way I feel, and it's always the way I've felt, frankly, in all of this stuff.

We need to get down there. We need to put teams together and we need to have a presence. There may be required a permanent presence in that area. I'm not the expert in that, and I don't pretend to be. I'm not an auditor and I'm not a criminal investigator. My job will be to focus, to manage, to hopefully motivate, and even lead—and lead is different than manage; a lot of people confuse those, but they are different—those auditors and investigators. I would like their input into how they would approach this as well. I know that something has to happen quite quickly.

Chair SNOWE. Thank you.

Senator Kerry.

Senator KERRY. Thank you, Madam Chairman.

Mr. Thorson, thank you for your pledges with respect to the approach to the job. We certainly appreciate that very much.

I was a little disappointed in your opening statement that you focused so significantly on the potential for fraud in the loans and fraud among the small businesses themselves and the homeowners in the Gulf region, but you didn't focus on the management problem itself within the SBA with respect to getting people on the

ground to do these things. I mean, part of avoiding fraud is having sufficient staff.

Mr. THORSON. Absolutely.

Senator KERRY. The staff has been cut. As you've just said, you're surprised there aren't auditors on the ground. Auditors? You've got 300,000 loans waiting to be processed.

It seems to me that before we start focusing on the fraud in the issuance of a loan, we'd better start issuing some loans.

Mr. THORSON. Yes, sir.

Senator KERRY. That's an oversight issue with respect to the SBA itself. What can you tell us today—I mean, is this going to be a priority when you get in there? It seems to me it's priority No. 1.

Mr. THORSON. It is. The reason it really didn't rise to that level in my statement is simply because fraud is much easier to understand, and it's much more easy to see in the press accounts and that sort of thing.

The other thing is, too—and I'm not moving away from your statement at all because I agree with it—but I haven't spent a day at SBA yet. I don't pretend to know exactly what the policies are. If I were going to start wading in with my opening statement, I want to know exactly what I'm saying.

The issues that you've raised—and efficiency of resources is another one that I have discussed with your staff as well—these are huge issues.

Senator KERRY. The question is—I misspoke. It's not 300,000. It's 130,000. There are 130,000 loans that are waiting to be processed. We've had the Administrator up here, and the Chair and I and others on the Committee months ago, on two occasions, once when we were assured that things were going to be put in place and a few weeks later, when they weren't, with more assurances.

I just want to call to your attention that the Members of this Committee on a bipartisan basis are deeply concerned. I'm confident you're going to hear from the Senator from Louisiana about what is and isn't happening down there.

Mr. THORSON. Yes, sir. As I said, I've read your correspondence, from both you and Senator Snowe, to the Agency. I think you've raised some excellent issues. You will not see me back away from any of those issues.

Do I have the perfect answer to solve some of those things? No, because I have heard the Agency give you one explanation, which is reasonable to some degree. They've talked about the limitations of computers systems. They've talked about being able to hire people. There are no people to hire that know the—I was in that hearing when you held that.

What we need to do is to be able to get the experts on the ground in that area to see what's happening, to see how the policies are being adhered to, what steps are being taken. I think what you're getting at, sir, is that what they're doing isn't—doesn't meet your standards of what you're expecting. If that's the case, then we need to be able to look at that as well and not only say, "is that true or not true," but "why, and what can be done to fix that."

I think, too, my effort would never be to work against the Administrator or SBA; but to work with him, but to be able to show why

we feel, as the experts in this field—which, again, I'm not, but I would be managing those people—and to come up with reasons as to how to make it better, how to make it work better, and to be able to stand before you and say, "this is what we found," and to see if you agree.

Senator KERRY. Sometimes, Mr. Thorson, the accountability job of the Inspector General is to measure whether or not the achievements and/or approaches of the particular agency are accomplishing their goals.

Mr. THORSON. Correct.

Senator KERRY. Not necessarily to provide the remedy. It may be that Congress has to provide the remedy, or the administration. If your job is to go over there, and the SBA is supposed to get these loans out, and they have said, "We're putting a program in place to do this and we pledge to you, Members of Congress, we're going to have these loans racing out," et cetera, et cetera, it seems to me your priority is to see if that's happening. If it's not, they're not accomplishing their goals.

Would you agree?

Mr. THORSON. Yes, I do. I think I see my job as maybe a little—one more step past that, but which certainly includes that part, but also making—and again, as you say, it's not my jump to make those things happen. I do think it is part of our task to provide recommendations as to where we see the weaknesses and where maybe you all can provide the fix.

Senator KERRY. I completely agree. No question that you are supposed to contribute to ways to provide effectiveness in management and so forth. We hope you will do that.

I want a pledge from you today that you understand and see this component that its not just the fraud and the homeowners that are going to be the targets here. The Agency itself has to be measured whether or not it is doing its job.

Mr. THORSON. I absolutely agree, sir. You have my pledge on that.

Senator KERRY. It's not a question of working with or against the Administrator, but the willingness to hold the Administrator accountable that will require you to say, you're not getting the job done.

Mr. THORSON. I absolutely agree with that. I do give you such a pledge.

Senator KERRY. I really don't want to belabor it, but I do want to just kind of get an extra question or two with respect to—if I may, Madam Chairman—just two quick things.

No. 1, budget cuts really are critical. Every Member of this Committee, I think, is concerned about what's happening to the budget. Budget cuts lead to fraud and abuse.

Mr. THORSON. Yes, they do.

Senator KERRY. If you're putting out $300 billion worth of Federal contracts but you don't have sufficient people to guarantee they're being put out properly or watch what's happening, boy, is that an invitation to abuse and fraud, and taxpayer dollars get wasted.

Can we count on you, should you be confirmed, to ensure that the SBA makes its own oversight requirements a priority? There

are requirements within the SBA for their oversight, and they're not doing it, necessarily, because they don't have the people.

Mr. THORSON. I absolutely agree with that, Senator, and that would be a priority, yes.

Senator KERRY. Finally, let me just—I'm trying to sort through this because—and Madam Chairman, could I ask unanimous consent that the two reports of the GAO just be placed in the record, as appropriate?

Chair SNOWE. Without, objection, so ordered.

[The GAO reports follow:]

United States General Accounting Office

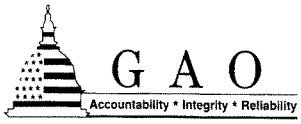
GAO

Report to the Chairman
Committee on Finance
U.S. Senate

May 1999

TAX ADMINISTRATION

Allegations of IRS Employee Misconduct



GAO/GGD-99-82

GAO

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

General Government Division

B-280651

May 24, 1999

The Honorable William V. Roth, Jr.
Chairman, Committee on Finance
United States Senate

Dear Mr. Chairman:

For years, the Congress has expressed concerns about the Internal Revenue Service's (IRS) management and treatment of taxpayers. We, and others, have chronicled IRS' struggle to modernize and have made scores of recommendations to improve IRS' operations and its service to taxpayers. Congressional concerns led to a June 1997 report[1] by the National Commission on Restructuring IRS and a series of hearings in 1997 and 1998 that focused on problems at IRS.

In April 1998, the Senate Committee on Finance held hearings on alleged misconduct by IRS employees in their treatment of other IRS employees and taxpayers. Witnesses testifying at the hearings alleged that (1) senior IRS managers did not receive the same level of disciplinary action as line staff; (2) the Deputy Commissioner of Internal Revenue delayed action on substantiated cases of employee misconduct until senior managers were eligible to retire; (3) IRS retaliated against whistleblowers and against taxpayers and their representatives who were perceived to be noncooperative; (4) IRS employees zeroed out or reduced proposed tax assessments for reasons not related to the merits of the cases; and (5) IRS discriminated against employees in the evaluation process on the basis of race or national origin in its Midwest District Office, which is headquartered in Milwaukee, WI.

You asked us to review these allegations and, in particular, to evaluate both the specific allegations made at the hearings and any underlying systemic or programmatic problems that needed to be resolved to protect the rights of taxpayers and IRS employees in these areas. This report provides information related to specific allegations regarding IRS senior managers and the Midwest District Office. It also brings together information bearing on the other allegations from our current and past work on systemic problems at IRS. Because some of the specific allegations involve taxpayer data that cannot be publicly disclosed, we are issuing to you at the same time as this report a separate, restricted letter

[1] A Vision for a New IRS, Report of the National Commission on Restructuring the Internal Revenue Service, June 25, 1997.

that discusses alleged improper zeroing out and retaliation against taxpayers.

We did our work in Washington, D.C., and Milwaukee between June 1998 and March 1999 in accordance with generally accepted government auditing standards. A complete description of the objectives, scope, and methodology for this report appears in appendix I. A summary of IRS' written comments on a draft of the report appears at the end of this letter.

Results in Brief

Available data showed significant differences between Senior Executive Service (SES) and line staff disciplinary cases in terms of dispositions and processing times. For example, a much higher percentage of SES cases than of lower-level cases was cleared or closed without action, and SES cases tended to take longer to complete. Also, IRS found that actions taken against lower-level employees more closely conformed to its established table of penalties than actions taken against higher-graded employees. However, there was no basis for a more direct comparison of the discipline imposed on senior managers and lower-level employees because SES and line staff offenses, as well as their associated mitigating and aggravating factors, were different. Our ability to make other comparisons between SES and line staff disciplinary cases was hindered by the lack of detailed and accurate data in connection with IRS' disciplinary case database.

Regarding the allegation that the Deputy Commissioner delayed action on senior manager misconduct cases until the managers were eligible to retire, we focused on actual retirements and did not reach general conclusions about eligibility to retire. We found no cases in which an individual who was ineligible to retire when an allegation was filed, retired while the case was pending with the Deputy Commissioner. However, cases we studied in depth were pending for 2 months to 4 years at the Deputy Commissioner's level. In addition, we estimated, on the basis of a random sample of IRS SES disciplinary files, that SES cases averaged almost a year from the time executive support staff received them until case closure, compared to a goal of 90 days. To address a variety of problems, including poor case-tracking procedures, inaccurate and incomplete records and files, and poor communication, IRS has started to revamp its entire disciplinary system.

We could not determine the extent of reprisal against whistleblowers because IRS did not track whistleblowing reprisal cases. The only systematic data available related to formal complaints filed with two independent review agencies—the U.S. Office of Special Counsel (OSC) and the U.S. Merit Systems Protection Board (MSPB). In fiscal years 1995

through 1997, OSC received 63 IRS whistleblower reprisal matters and obtained action from IRS favorable to employees in 4 cases. In the same time period, MSPB decided 45 initial appeals of whistleblowing reprisal allegations involving IRS, dismissing the majority of them but settling more than half of the remainder.

Regarding allegations of IRS retaliation against taxpayers, we previously reported that IRS information systems were not designed to identify, address, and prevent such taxpayer abuse.[2] In reviewing IRS databases for this report, we again found that IRS information systems provided limited and incomplete data on alleged revenue agent retaliation against taxpayers and their representatives.

With respect to allegations of improper zeroing out or reductions of recommended taxes by IRS managers, we found no evidence to support the allegations in the eight specific cases referred to us by the IRS employees who testified at the hearings. On the other hand, IRS did not systematically collect data on how much additional taxes recommended by auditors were zeroed out or reduced by IRS employees without a basis in law or IRS procedure. In particular, IRS had no data on supervisors' improperly limiting auditors' recommendations of additional tax before an audit was closed. Although our results were not a measure of improper reductions in recommended taxes, we recently reported that the majority of additional taxes recommended during audits was not assessed. We attributed this to many factors, including the complexity of the tax code and the overreliance on additional taxes recommended to measure audit results.

IRS has acknowledged equal employment opportunity (EEO)-related problems, including problems in hiring and promotion, in its Midwest District Office and has begun addressing them. After an Equal Employment Opportunity Commission administrative judge's finding that an IRS employee was a victim of discrimination, the district produced a climate assessment report. In addition, although a recent outside panel found no discriminatory hiring or promotion practices, its August 1998 report contained many recommendations related to several district problem areas, including the hiring and promotion processes. Since the report was

[2]Tax Administration: IRS Can Strengthen Its Efforts to See That Taxpayers Are Treated Properly (GAO/GGD-95-14, Oct. 26, 1994); Tax Administration: IRS Is Improving Its Controls for Ensuring That Taxpayers Are Treated Properly (GAO/GGD-96-176, Aug. 30, 1996); and Tax Administration: IRS Inspection Service and Taxpayer Advocate Roles for Ensuring That Taxpayers Are Treated Properly (GAO/T-GGD-98-63, Feb. 5, 1998).

issued, a new District Director was named who has stated her commitment to overcoming the district's contentious and long-standing EEO problems.

In general, IRS' lack of adequate information systems and documentation in the areas of employee discipline, retaliation against whistleblowers and taxpayers, and zeroing out of recommended taxes prevented us from doing a more comprehensive analysis of these issues. This lack of information hinders both congressional oversight and IRS management from addressing any problems in these areas. IRS has acknowledged the need for more complete and accurate program and management information on these issues.

The IRS Restructuring and Reform Act of 1998 included several provisions related to employee misconduct, abuse, and retaliation. As a consequence, IRS has taken steps intended to begin reform of its processes and data collection in the areas of employee discipline, retaliation, and the tax assessment process, among other things. We believe that it is important that IRS maintain adequate information systems and documentation so that employee and taxpayer complaints, including those related to retaliation, can be properly reviewed.

Disciplinary Actions for Senior Executive Service and Lower-Level Staff

Available data showed that case dispositions and processing times in disciplinary cases during the period of January 1, 1996, through June 30, 1998, differed for SES employees and lower-level, or general schedule (GS), staff. In addition, a 1997 IRS internal study found that actions taken against lower-level employees more closely conformed to the IRS table of penalties than actions taken against higher-graded employees.[3] However, because of dissimilarities in the types of offenses and incomplete case files, these data do not necessarily prove disparate treatment. Agencies must consider many factors, such as the nature and seriousness of the offense; the employee's job level and type of employment; whether the offense was intentional, technical, or inadvertent; the employee's past disciplinary record; and the notoriety of the offense or its impact upon the reputation of the agency, in deciding what penalty, if any, should be imposed in any given case. IRS recognized that problems have hindered the processing and resolution of employee misconduct cases and has begun revamping its disciplinary systems.

Background

For the period we studied, IRS tracked disciplinary cases for GS and SES employees in different systems. The Office of Labor Relations (OLR), which is the personnel office for non-SES staff, handled GS cases. It

[3] Guide for Penalty Determinations Report, IRS, Sept. 1997.

tracked these cases in the Automated Labor and Employee Relations Tracking System (ALERTS), although IRS officials told us that ALERTS data were often missing or incomplete. The Office of Executive Support (OES), which is the personnel office for IRS executives, handled SES cases. Although ALERTS was supposed to also track SES cases, OES tracked SES cases by using a log and monthly briefing reports. The monthly briefing reports were used to inform the Deputy Commissioner about the status of cases.

We selected the cases for our study of disciplinary actions for SES and lower-level staff as follows: For GS cases, we used ALERTS data for 22,025 cases received in, or closed by, OLR between January 1, 1996, and June 30, 1998. For SES cases, our information came from two sources: (1) a 70-case random sample of SES nontax misconduct case files that were active between January 1, 1996, and June 30, 1998;[4] and (2) for the same time period, 43 other SES nontax cases reported either in the logs or as "overaged"[5] SES cases in the monthly briefing reports. In total, we looked at 113 cases involving 83 SESers. Unless otherwise noted, all SES statistics presented in this section are based on the random sample. See appendix I for more information on how we selected the cases for our study.

We were unable to make many meaningful statistical comparisons between SES and GS employee misconduct cases for three reasons. First, we were able to collect more detailed data through our SES file review than from the ALERTS database used for GS cases. This was particularly true regarding dates on which important events occurred. As a result, we could not compare average processing time at each phase of the disciplinary process, although we were able to compare processing times from case receipt through case closure.

Second, the level of detail and accuracy of ALERTS data varied widely. Some IRS regions historically took ALERTS data entry more seriously than others did, according to an IRS memorandum, and cases contained varying levels of detail about case histories, issues, facts, and analyses. ALERTS had few built-in system controls to ensure data integrity. Instead, IRS relied on managers to ensure the accuracy of their subordinates' work.

Third, some data were missing for the majority of the cases tracked in ALERTS. For example, we could not analyze the frequency with which

[4]We excluded employee tax cases because they were inherently different from the cases and issues raised during the April 1998 Senate Finance Committee hearings.

[5]IRS defined overaged cases as those cases pending in OES for more than 90 days.

final dispositions were less severe than proposed dispositions because both pieces of information were available for only about 13 percent of the ALERTS cases. Because officials said that ALERTS was OLR's means of recording information on lower-level disciplinary cases, we used it to the extent that it had information comparable to what we collected on SES cases.

Comparisons Between SES and Lower-Level Misconduct Cases

Available data showed that processing time and frequency and type of case dispositions differed for SES and lower-level staff. On average, from OES' or OLR's receipt of a case until case closure, SES cases, on the basis of our 70-case random sample, lasted almost a year (352 days) and lower-level cases lasted less than 3 months (80 days).

We estimated that the largest difference between SES and GS case dispositions occurred in the closed without action (CWA) and clearance categories. As shown in table 1, the dispositions in 73 percent of SES cases were CWA or clearance, versus 26 percent for GS cases. CWA is to be used to close a case when the evidence neither proves nor disproves the allegation(s). A disposition of clearance is to be used when the evidence clearly establishes that the allegations are false. In practice, neither disposition results in a penalty. The actual breakdown between the two dispositions is as follows: for SES cases, 61 percent were CWA and 12 percent were clearance; for GS cases, 24 percent were CWA and 2 percent were clearance.

Table 1: Percentages of Closed SES and Lower-Level Misconduct Cases Receiving Various Dispositions

Disposition	Percentage of sampled SES cases	Confidence interval for SES cases[a]	Percentage of GS cases[b]
Clearance or closed without action	73	63.4 - 83.4	26
Caution letter	0	0 - 5	3
Oral or written counseling	9	4.5 - 17.0	13
Reprimand	2	0.4 - 7.9	9
Suspension	0	0 - 5	9
Removal	0	0 - 5	5
Retired/Resigned	9	4.5 - 17.0	11
Other[c]	7	3.2 -14.8	25

[a]The confidence level for these intervals was 95 percent.

[b]Does not add to 100 percent due to rounding.

[c]For GS cases, "other" includes admonishments, leave restriction, reassignment, alternative discipline, cases forwarded to Inspection, missing and miscoded cases, and other dispositions. For SES cases, "other" includes missing and miscoded cases.

Sources: GAO analysis based on sample of SES cases and information from IRS' ALERTS.

Table 1 outlines in order of severity the frequency with which available data indicate that various dispositions were imposed for SES and lower-

level staff. SES data are based on the 56 closed cases in our 70-case sample. GS data are based on 15,656 closed cases in ALERTS.[6] Ninety-five-percent confidence intervals for the SES data are presented to more accurately portray our findings. Using these confidence intervals, the rates of occurrence differed between SES and GS cases for dispositions of clearance and CWA, reprimand, suspension, and other. However, using 95-percent confidence intervals and eliminating the CWA or clearance category from the analysis, the rates of occurrence between SES and GS cases were similar for all dispositions, except oral or written counseling and retired/resigned. In any case, we will discuss later in this report that differences in dispositions of SES and GS cases do not necessarily mean that the dispositions were inappropriate or that disparate treatment occurred.

We also analyzed disciplinary actions for an additional 43 SES cases. Because these cases were not randomly selected, the results may not be representative. Of the 43 cases, we found 9 in the more serious categories—6 instances of counseling, 1 reprimand, 1 suspension, and 1 removal.

Factors Affecting Case-Processing Time and Dispositions

As further detailed in the upcoming section of this report on alleged case-processing delays by the Deputy Commissioner, SES cases took a long time to close for many reasons. These reasons included poor case-tracking procedures, inadequate file management, and poor communication among agency officials involved in the disciplinary process. We do not know to what extent, if any, these difficulties contributed to differences in processing times between SES and GS cases.

Many factors can affect the discipline imposed in a particular case. These factors include the nature and seriousness of the offense; the employee's job level and type of employment; whether the offense was intentional, technical, or inadvertent; the employee's past disciplinary record; and the notoriety of the offense or its impact upon the reputation of the agency. Collectively, these factors are components of what is known as the Douglas Factors, and they must be considered in determining the appropriate penalty in a case.[7] See appendix II for a listing of the Douglas Factors.

[6]Excludes duplicate cases and nondisciplinary dispositions.

[7]Douglas v. Veterans Administration, 5 M.S.P.R. 280 (1981).

Not all of the Douglas Factors will be pertinent in every case, and, while some factors will weigh in the employee's favor (mitigating factors), others may weigh against the employee (aggravating factors). IRS officials told us that lower-level actions tend to be more straightforward than SES actions, with fewer mitigating factors. Since mitigating factors tend to reduce the level of discipline imposed, this could partially explain why penalties might be imposed differently in lower-level cases than in SES cases.

We found that allegations against SES employees were usually reported to a hotline, the Department of the Treasury's Office of Inspector General (OIG), or the IRS Inspection Service. Because complaints against SES employees can be anonymous, this anonymity can affect IRS' ability to follow up on a complaint or investigate it thoroughly. In contrast, IRS officials told us that GS cases were generally filed by managers about their subordinates. In these cases, the complainant was known and generally provided concrete evidence to support the allegation.

Further, typical issues surrounding lower-level cases may be less complicated or easier to successfully investigate than those involving SES employees. Table 2 outlines in more detail the most common issues in SES and lower-level staff cases. SES data are based on our 70-case sample. GS data are based on 22,025 cases in ALERTS. We subjectively classified the issues in SES cases, and our classifications may not be precise. Overall, we found that the most common issue in SES cases was prohibited personnel practices,[8] while time and attendance was the most common issue in GS cases.

Table 2: Most Frequently Cited Issues in SES and GS Disciplinary Cases

Cases	Most common issue	Second most common issue	Third most common issue[a]
SES sample	Prohibited personnel practices	Misuse of funds/property; fraud, waste, and abuse	Procurement issues; lying/falsifying documents; abuse of position/authority; preferential treatment
GS	Time and attendance	Unauthorized access to taxpayer information	Unacceptable job performance

[a]There was a four-way tie among SES cases.

Sources: GAO analysis based on SES case file review and issue data from IRS' ALERTS.

[8]Defined as actions that, by law, may not be taken by any employee who can take, direct others to take, recommend, or approve any personnel actions. Examples include discrimination, coercion of political activity, and nepotism. 5 U.S.C. 2302(b).

IRS Study of Penalty Guide Effects

In 1994, in response to an internal IRS study reporting a perception that managers received preferential treatment in disciplinary matters, IRS created a table of penalties, the Guide for Penalty Determinations.[9] The purpose of the guide was to ensure that decisions on substantiated cases of misconduct were appropriate and consistent throughout IRS. In 1997 and 1998, IRS studied the effect of the guide on GS and SES employees and found that

- actions taken against lower-graded employees more closely conformed to the guide than those taken against higher-graded employees (see table 3);
- for GS employees overall, 91 percent of disciplinary actions conformed to the guide, versus 74 percent for SES employees;
- when disciplinary actions did not conform to the guide, the actions were below the guide's prescribed range 93 percent of the time for GS employees overall, versus 100 percent of the time for GS-13 through GS-15 and SES employees; and
- if admonishments were included as part of reprimands, conformance with the guide approached 100 percent for GS-13 through GS-15 employees.

Table 3: Degree With Which Disciplinary Action Conformed to Guide for Penalty Determinations, 1994-97

Employee level	Degree of conformance with the penalty guide
GS-2 through GS-7	92% - 93%
GS-8 through GS-12	88 - 91
GS-13 through GS-15	77 - 87
All SES[a]	74

Note: Nonconformance with the penalty guide does not necessarily mean that a particular penalty was inappropriate.

[a]IRS reviewed 164 executive cases. Of these, 43 cases had dispositions that were subject to the provisions of the guide.

Source: Report of the Employee Complaints Analysis Group, IRS, 1998.

The IRS study and IRS officials agreed that the guide had limitations and no longer met IRS needs. Specifically, the guide covered all employees but did not address statutory and regulatory limitations that restricted management's ability to impose disciplinary suspensions on SES employees. IRS officials said that governmentwide, there was no level of discipline available for SES employees that was more severe than a reprimand but less severe than a suspension of at least 15 days.[10] In contrast, GS employees could have received suspensions of 14 days or less. While the guide prescribed a penalty range of "reprimand to suspension," the only option for SES employees, because of the statutory

[9]Report of the Double Standard Study Group, IRS, May 1992.

[10]5 U.S.C. 7542 and 5 C.F.R. 752.601(b).

limitations against suspensions of less than 15 days, was a reprimand if management wished to impose a penalty, but not the harshest available penalty. IRS officials also told us that in certain cases, they might have imposed discipline in between a reprimand and a 15-day suspension had they had the option to do so. According to IRS officials, IRS' 1995 attempt to have the Office of Personnel Management deal with this issue was unsuccessful. Statutory and regulatory requirements could partially explain why reprimands might have been imposed when a harsher disciplinary action might have seemed more appropriate.

Applying to employees at different levels, the IRS penalty guide was constructed with very broad recommended discipline ranges to provide for management discretion. However, one IRS study pointed out that, in some instances, this rendered the guide useless (e.g., when the penalty range was "reprimand to removal").[11]

IRS Is Making Changes to Its Complaint System

IRS created a disciplinary review team in September 1998. Among other things, the team was to

- develop an action plan that addressed case handling, complaint systems, and employee awareness;
- review and revise IRS' Guide for Penalty Determinations; and
- develop a process to review and monitor complaints.

As of March 1999, the team was proposing a new integrated IRS complaint process. Its intent was to overcome problems with complaint processing systems' not (1) communicating or coordinating with each other, (2) capturing the universe of complaints, (3) specifically tracking or accurately measuring complaints, and (4) following up on complaints to ensure that appropriate corrective action had been taken. The team was proposing a 26-person Commissioner's Review Group to, among other things, manage and analyze complaints sent to the Commissioner of Internal Revenue, monitor other IRS complaint systems, and coordinate with the systems' representatives. The team was also redesigning the penalty guide.

[11]For the 51 offenses listed in the penalty guide, 15 offenses (or 29 percent) had a range of "reprimand to removal" or "admonishment to removal."

Alleged Delays by IRS Deputy Commissioner on Senior Executive Service Misconduct Cases

On the basis of our review of SES cases, we did not find a case in which an individual who was ineligible to retire at the time an allegation was filed, retired while the case was pending with the Deputy Commissioner. However, we found cases that spent up to 4 years at this stage in the disciplinary process and cases that stalled at various points throughout the process. Although OES' goal for closing an SES case was 90 days, on the basis of our random sample, cases averaged almost 1 year for OES to close. Further, IRS had poor case-tracking procedures, inadequate file management, missing and incomplete files, and poor communication among officials involved in the disciplinary process.

Background

Because IRS' 1990 and 1994 written SES case-handling procedures were out of date, IRS officials described the operable procedures to us.[12] During the period covered by our review, OES handled SES misconduct cases. Its goal for closing a case was 90 days from its receipt of a case. Once OES received a case, it was to enter it into ALERTS, although it did not always do this, and prepare a case analysis. The case analysis and supporting documents were then to be forwarded to the appropriate Regional Commissioner, Chief, or Executive Officer for Service Center Operations, who was to act as the "recommending official." Within 30 days, the recommending official was to review the case with the help of local labor relations experts, develop any additional facts deemed appropriate, and return a case report to OES, including a recommendation for disposition.

If OES disagreed with the report for any reason, it was to include a "statement of differences" in its case analysis. OES was to forward the field report and the OES analysis to the Deputy Commissioner's office for concurrence or disapproval. If the Deputy Commissioner concurred with the proposed disposition, the recommending official could take action. If the Deputy Commissioner did not approve, he could impose a lesser disposition or return the case to OES for further development.[13] IRS executive case-handling procedures did not define a time period within which the Deputy Commissioner was to act on case dispositions.

We collected information on SES cases from two sources: (1) the five specific cases mentioned during the April 1998 Senate Finance hearings, and (2) a 70-case random sample of the SES misconduct case files as previously described, plus 43 more cases from OES tracking logs and

[12]Offices and positions in existence when the procedures were written had changed or disappeared but were still official links in the processing chain.

[13]IRS officials told us that, procedurally, it would be difficult for the deciding official to impose a more severe penalty than what was proposed.

monthly briefing reports, for a total of 113 cases. These 113 cases involved 83 individuals. Again, see appendix I for more details on how we selected the cases to study.

No Cases Showing Retirement Linked to Deputy Commissioner Delays in Case Processing

Of the 113 SES cases we reviewed, we did not find a single instance in which an individual who was ineligible to retire at the time the allegation was filed, retired while the case was pending with the Deputy Commissioner. Overall, of the 83 individuals involved in the 113 cases, 25 people, or 30 percent, had retired from IRS by December 31, 1998.[14] Of these 25 people, 13 retired before their cases were closed or the cases were closed because the individuals retired. At the time of retirement, cases for 2 of the 13 people were pending in the Deputy Commissioner's office, but both of these individuals had been eligible to retire at the time the complaints against them were originally filed. Cases for the remaining 11 of the 13 people either were still being investigated or were pending in OES, that is, they had not yet reached the Deputy Commissioner's office. In doing our analyses, we focused on actual retirements and did not reach general conclusions about eligibility to retire.

As table 4 shows, of the five executive cases mentioned during the April 1998 hearings, two of the executives were already eligible to retire when the allegations against them were filed. We refer to the executives in the five cases as Executives A through E. One of the two eligible executives—Executive B—was still an IRS employee as of September 30, 1998. The other—Executive D—retired while, in OES' view, his case was pending in the Deputy Commissioner's office.[15] Of the three individuals who were not eligible to retire when the allegations against them were filed, one retired 16 months after his case was closed. The other two executives, one of whom was not found culpable, were still employed by IRS as of September 30, 1998.

[14]The 25 individuals do not include people for whom specific retirement dates were unavailable or individuals whose cases were received in OES after they had retired.

[15]Executive D was transferred about 7 months after the Inspection investigation was completed. The Deputy Commissioner considered the case closed with the individual's transfer, but OES was unaware of the Deputy Commissioner's view and did not formally close the case until 3 months after Executive D retired, or 35 months after the transfer.

Table 4: Information on the Five Misconduct Cases Cited at the April 1998 Senate Finance Committee Hearings

SESer	Employment status at our September 30, 1998, cutoff date	Retirement status at time of allegation	Case pending with Deputy Commissioner (months)	Case outcome
A	IRS employee	Not eligible to retire	*	Not found to be culpable for violation
B	IRS employee	Eligible to retire	2	Counseled, confirmed in writing
C	Retired	Not eligible to retire	18	Counseled
D	Retired	Eligible to retire	*	Transferred
E	IRS employee	Not eligible to retire	48	Counseled, confirmed in writing

*Disciplinary file did not document the duration of the Deputy Commissioner's review.

Sources: GAO analysis based on IRS misconduct case files and retirement eligibility information.

IRS records showed that the misconduct cases spent from 2 months to 4 years at the Deputy Commissioner level. See appendix III for more details about the five cases.

Case Processing Not Timely

As shown in table 5, on the basis of our random sample, the total processing time for SES misconduct cases averaged 471 days (almost 16 months) from the date the complaint was filed until the case was closed. Most of this time involved OES case analysis and referral to the recommending official for inquiry (214 days, or about 7 months) and investigation by the recommending official (124 days, or more than 4 months). These averages exceeded IRS' most recent, written case-processing time guidelines, which were 14 and 30 days, respectively. The average total time from OES' receipt of a case to the case's closure was 352 days, compared to a goal of 90 days. As previously mentioned, there was no targeted time frame for the Deputy Commissioner's review. However, on average, cases spent 42 days at this level.

Table 5: Processing Time at Selected Stages in the Disciplinary Process for SES Misconduct Cases

Stages of process	Percentage of sample cases with information[a]	Median number of days	Mean number of days	Required number of days	Range of days
Complaint filed to OIG/Inspection beginning investigation	21	41	60	10-15	0 - 280
Complaint filed to OIG/Inspection declining to investigate	66	40	57	10-15	0 - 306
OIG/Inspection starting investigation to referral to IRS	21	123	130	No standard	7 - 355
OES receipt to transmittal to recommending official (RO)	60	161	214	14	43 - 690
RO's receipt of case to RO's completion of inquiry	56	99	124	30	13 - 514
OES transmittal to deciding official (DO) to DO's decision	57	30	42	No standard	2 - 143
DO's decision to case closure	57	0	12	No standard	0 - 202
OES receipt to case closure	79	252	352	90	13 - 1,275
Overall time: complaint filed to case closure	**79**	**390**	**471**	**No standard**	**104 - 1,467**

Note: Ninety-five-percent confidence intervals surrounding the mean number of days for all processing stages were less than plus or minus 10 percent.

[a]Some percentages were relatively low because not all cases went through every phase, case files did not always include all dates, and open cases still had processing phases to go through.

Sources: GAO analysis based on IRS misconduct case data and executive case-handling procedures.

In addition, we found that some cases took a particularly long time to be resolved. For example, in our sample cases, from the date the complaint was filed to the date the case was closed, 8 cases took at least 2 years, an additional case took more than 3 years, and still another case took longer than 4 years.

In 1992, IRS acknowledged that the best way to prevent employees from retiring before their cases closed was to improve timeliness.[16] Although we found no cases in which individuals ineligible to retire when allegations

[16]IRS' Program to Combat Senior-Level Misconduct: Getting Stronger but Still a Long Way to Go, Forty-First Report by the Committee on Government Operations, Nov. 23, 1992.

were made retired with the case pending before the Deputy Commissioner, the longer it takes to close cases, the more likely that individuals would retire or resign while their cases were open.

Problems With the SES Misconduct Case-Handling Process

Our review and a recent IRS task force report identified numerous problems with the executive misconduct case-handling process.[17] These problems included inadequate staffing, poor communication, inaccurate and incomplete records and files, outdated procedures, conflicts over proposed case dispositions, and internal disagreement about case investigations. These problems contributed to the lengthy case-processing times in the available data and case files.

Lack of IRS Staff Resources

According to IRS officials, IRS' downsizing a few years ago significantly affected OES and field staff resources. From late 1996 through early 1998, OES devoted only one staff year to executive misconduct cases. The staff year was divided between the Director and one employee. In mid-1998, the Director moved to Labor Relations, and the employee retired, leaving OES with no resident expertise. Previously, four or five case experts handled executive cases. In total, according to an IRS official, the office was understaffed for about 18 months, which caused a case backlog. However, the new Chief of OES was able to bring the staffing level up to eight, including two individuals with employee relations backgrounds to act as team leaders. She also used detailees and a technical contractor to reduce the case backlog.

The understaffing issue also extended to the labor relations functions in the regions. These functions supplied the staff that recommending officials used to investigate misconduct cases. When the regional offices were consolidated several years ago, they lost their labor relations functions as well as a central repository for program administration and expertise.

IRS did not enter executive misconduct cases into ALERTS from late 1996 through early 1998. IRS officials told us they did not have enough labor relations experts to properly track cases on ALERTS because the system required significant detail about each case. Instead, it tracked these cases using logs and monthly briefing reports. OES also used the briefing reports to inform the Deputy Commissioner of case status. IRS officials acknowledged that these independent systems often disagreed with each other about the details and status of the cases.

[17] Task Force to Review Handling of Executive, Grade 15 and Inspector General Referrals and Investigations, IRS, July 28, 1998.

Poor Communication

Our review found that poor communication among IRS support staff, the Deputy Commissioner's office, IRS Inspection, and OIG contributed to case-processing delays. As previously mentioned, the Deputy Commissioner considered one case to be closed with the transfer of the individual, but OES was not told to formally close the case. In another instance, the Deputy Commissioner told us that he inadvertently allowed a case to be lost in the system. Case information in the ALERTS, OES, and IRS Inspection tracking systems was also found to be inconsistent and inaccurate in many instances. For example, according to IRS officials, cases recorded as "overaged" in the IRS Inspection system were recorded as "closed" by the field offices, leading to confusion among officials as to whether a case was open or closed and where a particular case was pending at a given time.

An internal IRS study found that many cases had timeliness problems, especially cases that had been referred to IRS from OIG. In certain instances, cases stayed at a particular phase in the process for months before an OES employee inquired about their status. In one instance, for nearly 2 years, OES did not follow up on the status of an OIG investigation. IRS officials told us that these problems occurred primarily because IRS had no contact person for OIG cases before early 1997, and because OES lacked staff resources to properly monitor cases.

Administrative Practices That Raised Concerns

Our review identified several concerns surrounding IRS' files, records, and miscellaneous procedures for executive misconduct cases. Examples included the following:

- Poor filing. Executive misconduct cases were to be filed alphabetically. Several times, we happened upon misfiled cases only because we went through all of the files to draw our sample. Also, in one instance, a closing letter addressed to the executive involved in a case was filed instead of being mailed to the individual. It took nearly 5 months for the error to be discovered and rectified.

- Missing files and records. We requested eight case files for our review that IRS could not provide, even after more than 4 months.

- Incomplete files. In some cases, the case files did not document important information, such as dates, transmittal memorandums, and final case dispositions. In one instance, the case file consisted of a single E-mail message. The case was serious enough to warrant suspending the individual.

- Noncompliance with procedures. In several instances, field staff imposed discipline before the Deputy Commissioner had concurred with the proposed action. Several files contained memorandums to the field staff, reminding them not to impose discipline or close a case until the Deputy Commissioner had indicated his approval. Further, as mentioned in appendix III, a premature disposition occurred in one of our case studies.

Outdated Procedures

According to two 1998 IRS internal studies, outdated procedures led to inefficient case handling and confusion as to who was responsible for what. Because of regional and district consolidations and a national office restructuring, the written, 1994 case-handling procedures no longer accurately depicted the proper flow of cases. Although procedures were informally adjusted and work kept moving, it was not efficient. As a result, ad hoc procedures were developed in each region, leading to communication problems between the regions and the national office. IRS recognized this problem in March 1998 and completed a draft of new case procedures in July 1998. During that time, the Internal Revenue Service Reform and Restructuring Act of 1998[18] established the Treasury Inspector General for Tax Administration (TIGTA), and procedures were again revised to accurately depict TIGTA's role. According to IRS officials, draft procedures were sent to IRS field offices for comment in mid-March 1999.

Internal Disagreements

Another factor contributing to case-processing delays was internal disagreement surrounding the proper level of discipline to impose in particular cases. In our case studies, we noted instances in which internal disputes significantly lengthened case-processing times.[19] OES officials told us that this situation occurred much more frequently in the past. However, over the past few years, IRS has made a concerted effort to resolve disputes below the Deputy Commissioner level.

As shown in table 6, in the cases involving Executives C and D, disagreements were serious. In fact, they warranted formal statements of differences. In each of these two cases, OES endorsed a stronger level of discipline than that suggested by the recommending official. In the case of

[18]P.L. 105-206.

[19]See appendix III for information on these disagreements.

Executive E, IRS officials disagreed among themselves over the facts of the case. Although an IRS Internal Security investigation confirmed the allegations, the Deputy Commissioner was not comfortable with the allegations' correctness. However, he eventually agreed that the allegations had some merit. The Deputy Commissioner issued a letter of counseling 5-½ years after the complaint was filed, which was more than 4 years after he received the case.

Table 6: Disputes Surrounding Case Dispositions in Three Executive Misconduct Cases

SESer	Recommending official's proposed disposition	OES' original proposed disposition	Final disposition
C	Close without action	Letter of reprimand [a]	Closed without action, but employee was counseled
D	Counseling	15-day suspension and consideration of transferring the employee	Transferred, according to Deputy Commissioner; according to OES, closed without action "administratively" due to retirement[b]
E	Letter of reprimand	Letter of reprimand[c]	Letter of counseling

[a]OES subsequently changed its position and recommended a disposition of "close without action."

[b]See footnote 15 of this report.

[c]The proposed disposition was later changed to "letter of reprimand or letter of counseling."

Source: GAO analysis based on IRS misconduct case files.

Recent IRS Actions

As of March 1999, an IRS disciplinary review team was proposing changes to overcome problems with complaints processing. One of the units of its proposed Commissioner's Review Group was to provide labor relations support for SES and other cases. This unit would have 11 employees. In addition, the Commissioner's Review Group would have a contractor available to supplement it and support field investigations when management believed help was needed. As previously mentioned, the group would also be responsible for overcoming communication and coordination problems among complaint-processing systems.

Number of Whistleblowing Reprisal Cases and Extent of Information on Alleged IRS Retaliation Against Taxpayers

IRS did not comprehensively collect and analyze information on reprisals against IRS employee whistleblowers or on IRS retaliation against taxpayers. Some information was available on the number of IRS-related whistleblowing reprisal cases resolved by the two agencies responsible for considering such cases. For example, one of the agencies, OSC, received 63 IRS whistleblower reprisal matters over the fiscal years 1995 through 1997 and obtained action from IRS favorable to employees in 4 cases. Concerning allegations of IRS retaliation against taxpayers, we reported in 1996 and 1998 that IRS did not systematically capture information needed to identify, address, and prevent such taxpayer abuse. During this review, we also found limited and incomplete IRS information of past revenue agent retaliation against taxpayers.

The IRS Restructuring and Reform Act of 1998 included several provisions related to abuse or retaliation against taxpayers, their representatives, or IRS employees. As of March 1999, the IRS disciplinary review team was proposing how data needed to fulfill the act's requirements would be assembled.

Reprisals Against Whistleblowers

It is against the law to take a personnel action as a reprisal against a whistleblower.[20] More specifically, an employee with personnel authority is not allowed to take, fail to take, or threaten a personnel action against an employee because the employee made a protected disclosure of information. Protected disclosures include disclosures that an employee reasonably believes show a violation of law, rule, or regulation; gross mismanagement; gross waste of funds; or an abuse of authority.

If federal employees believe they have been subject to reprisal, they may pursue their complaint through the agency where they work. Alternatively, they may direct their complaint to OSC or MSPB.

We could not determine the extent of reprisal against whistleblowers because IRS did not track information on whistleblower claims of reprisal. According to a knowledgeable IRS official, until recently, the ALERTS database did not have a code to capture information on retaliation associated with individuals, including reprisal against whistleblowers. However, OSC and MSPB provided the number of complaints filed with them.

Office of Special Counsel Cases

Under the Whistleblower Protection Act of 1989, OSC's main role is to protect federal employees, especially whistleblowers, from prohibited

[20] 5 U.S.C. 2302(b)(8).

personnel practices. In this role, OSC is to act in the interests of the employees by investigating their complaints of whistleblower reprisal and initiating appropriate actions. Whistleblowing employees may file a complaint with OSC for most personnel actions that are allegedly based on whistleblowing.

As shown in table 7, between fiscal years 1995 and 1997, OSC received 63 whistleblowing reprisal matters related to IRS, compared to 2,092 for the federal government as a whole. However, OSC concluded that a much smaller number of IRS and governmentwide reprisal matters involved potentially valid statutory claims and therefore warranted more extensive investigation. OSC closed cases without further action for many reasons, including lack of jurisdiction over an agency or employee, absence of an element needed to establish a violation, and insufficient evidence.

Table 7: OSC Whistleblower Reprisal Matters for Fiscal Years 1995-97

Category	IRS	Governmentwide
Matters received	63	2,092
Matters referred for field investigation	13	621
Actions favorable to employees	4	237

Source: OSC.

Since IRS had about 100,000 employees during this period, the ratio of matters received to the number of employees was less than a tenth of 1 percent. Similarly, although OSC received whistleblowing reprisal matters from throughout the federal government, the number of matters received was an extremely small percentage of the civilian employee federal workforce that numbered almost 2 million people.

As table 7 further shows, at times both IRS and the federal government took "favorable actions" as a result of OSC investigations. In general, favorable actions are those that may directly benefit the complaining employee, punish the supervisor involved, or systematically prevent future questionable personnel actions. Agencies take these actions after receiving a request from OSC or with knowledge of a pending OSC investigation. The four favorable actions taken by IRS between fiscal years 1995 and 1997 entailed removing disciplinary letters from a personnel file, correcting an employee's pay level, presenting a performance award, and promoting an employee retroactively and providing back pay.

Merit Systems Protection Board Cases

Employee complaints of whistleblowing reprisal may reach MSPB in two ways. First, if employees do not obtain relief through OSC, they may appeal to MSPB. Second, employees may appeal directly to MSPB without

first going through OSC. They may do this for actions including adverse actions, performance-based removals or reductions in grade, denials of within-grade salary increases, reduction-in-force actions, and denials of restoration or reemployment rights. MSPB categorizes both types of appeals as "initial appeals."

MSPB administrative judges throughout the country decide initial appeals. The judges either dismiss the cases or decide them on their merits. Common reasons for dismissing cases are that they do not raise appealable matters within MSPB's jurisdiction or that they are not filed within the required time limit. The parties to the dispute also may enter into a voluntary settlement, sometimes with assistance from the judge. Cases not dismissed or settled are adjudicated on their merits. Possible outcomes are that the agency action may be affirmed or reversed or the agency penalty may be mitigated or otherwise modified.

A party dissatisfied with a case decision may file a "petition for review" by MSPB's three-member board. The board may grant a petition if it determines that the initial decision was based on an erroneous interpretation of law or regulation or if new and material evidence became available. It may dismiss a petition that is untimely, withdrawn by the parties, or moot. Petitions may also be denied or settled.

As with OSC, the number of whistleblowing reprisal decisions issued by MSPB was very small compared to the size of the IRS and federal workforces. As shown in table 8, for fiscal years 1995 through 1997, MSPB decided 45 initial appeals of whistleblowing reprisal allegations involving IRS. Similar to MSPB's rulings involving the rest of the federal government, MSPB dismissed the majority of initial appeals involving IRS and denied the majority of petitions for review. However, settlements occurred in more than half of the initial appeals that were not dismissed, which could mean that employees were getting some relief. MSPB also occasionally remanded petitions for review, that is, sent them back for further consideration. MSPB ordered IRS corrective action (canceling an employee's removal and mandating back pay) in one initial appeal case when due process measures unrelated to reprisal were not followed. To our knowledge, except for this case, MSPB did not reverse any IRS actions regarding alleged whistleblower reprisal matters over the 3-year period. For government initial appeals as a whole, MSPB ordered agency

corrective action 11 times and otherwise reversed agency actions in 24 instances.[21]

Table 8: Number of MSPB Decisions Covering Whistleblower Disclosures for Fiscal Years 1995-97

Decision	IRS	Treasury	Governmentwide
Initial appeals			
Dismissed	27	63	882
Corrective action not ordered	1	6	70
Corrective action ordered	1	3	11
Settled	11	22	324
Affirmed	4	11	127
Reversed	0	0	24
Modified/Mitigated	1	4	21
Total	**45**	**109**	**1,459**
Petitions for review			
Dismissed	1	1	23
Settled	0	2	14
Denied	13	23	229
Denied then reopened	0	3	26
Granted - affirmed	0	2	10
Granted - reversed	0	0	7
Granted - remanded	3	5	32
Granted - mitigated	0	1	1
Granted - other	1	1	4
Other	0	0	3
Total	**18**	**38**	**349**

Sources: Information compiled by GAO from MSPB, IRS, and the Internet.

Extent of Information on IRS Retaliation Against Taxpayers

Before the IRS Reform and Restructuring Act of 1998, IRS did not systematically collect information on retaliation against taxpayers. As we have previously reported,[22] IRS information systems were designed for tracking disciplinary and investigative cases or correspondence and not for identifying, addressing, or preventing retaliation against taxpayers. The systems contained data elements that encompassed broad categories of employee misconduct, taxpayer problems, and legal action. Information in the systems related to allegations of taxpayer abuse was not easily distinguishable from information on allegations not involving taxpayers.

[21] Although we did not have any governmentwide statistics for 1998, we did have 1998 information for IRS. The only decisions in these cases that could have been construed to be favorable to the original complainants were 6 settlements out of the 25-case total.

[22] GAO/GGD-95-14, GAO/GGD-96-176, and GAO/T-GGD-98-63.

Consequently, we found limited information on potential taxpayer abuse in IRS information systems, as shown in table 9.[23]

Table 9: IRS Information on Retaliation Against Taxpayers

Database	Results of GAO queries
Internal Security Management Information System	IRS found information on two cases of confirmed retaliation in 4 years but said coding in database could not ensure comprehensiveness.
Automated Labor and Employee Relations Tracking System	Until recently, database did not include a code for retaliation for cases associated with individuals.
Problem Resolution Office Management Information System	Database did not include a code for retaliation.
Executive Control Management System	IRS case summaries described four cases as taxpayer retaliation during 1 year for this system, in existence since mid-1997. According to IRS, the system's coding was becoming more specific.

Source: GAO analysis of various IRS databases.

Restructuring Act Reporting Requirements

Recent changes in the law and IRS' progress on information systems are intended to improve IRS' ability to determine the extent to which its employees might have retaliated against taxpayers or employees for whistleblowing. Enacted in July 1998, the IRS Restructuring and Reform Act of 1998 included several provisions related to abuse or retaliation against taxpayers, their representatives, or IRS employees.

Section 1203 of the act provided for firing IRS employees who commit any 1 of 10 acts. For example, the act required the Commissioner of Internal Revenue to fire any IRS employee for

"violations of the Internal Revenue Code of 1986, Department of Treasury regulations, or policies of the Internal Revenue Service (including the Internal Revenue Manual) for the purpose of retaliating against, or harassing, a taxpayer, taxpayer representative, or other employee of the Internal Revenue Service" ...or ... "threatening to audit a taxpayer for the purpose of extracting personal gain or benefit."

The act also required the Treasury Inspector General for Tax Administration to include in its annual report summary information about any termination under section 1203 or about any termination that would have occurred had the Commissioner not determined there were mitigating factors. In March 1999, the disciplinary review team previously described was proposing that the Commissioner's Review Group report these data to the Inspector General as well as broader data on the number of taxpayer complaints and the number of taxpayer abuse and employee

[23]For information on specific allegations of retaliation against taxpayers, see Tax Administration: Investigation of Allegations of Taxpayer Abuse and Employee Misconduct Raised at Senate Finance Committee's IRS Oversight Hearings (GAO/OSI-99-9R, May 24, 1999).

misconduct allegations. The group would collect, consolidate, and validate data from existing systems and obtain supplemental information to fill gaps. However, according to the team, the group would have to qualify the initial reports to the Inspector General, waiting for data reliability to be established.

Alleged Improper Zeroing Out or Reduction of Recommended Tax

With respect to allegations of improper zeroing out or reductions of recommended tax by IRS managers, we found no evidence to support the allegations in the eight specific cases referred to us by the IRS employees who testified at the hearings. On the other hand, IRS does not systematically collect data on the extent to which additional taxes recommended by IRS auditors are zeroed out or reduced without a basis in law or IRS procedure. While there are no data on improper reductions, there are data on IRS recommendations of additional tax that were not ultimately assessed. On the basis of such data, we recently reported that the majority of recommended additional taxes was not assessed. We attributed this result to a variety of factors, including the complexity of the tax code and the overreliance on taxes recommended as a measure of audit results.

Background

IRS' process for doing audits of taxpayers' returns and closing related disputes over additional recommended taxes has several steps. In an audit, an IRS auditor usually reviews the taxpayer's books and records to determine compliance with tax laws and identify whether the proper amount of tax has been reported. To close an audit, the auditor may recommend increasing, decreasing, or not changing the tax reported. If a taxpayer disagrees with the recommendation at the close of the examination, the taxpayer may request an immediate review by the auditor's supervisor.

If the taxpayer agrees with the recommended additional tax or does not respond to IRS' notices of examination results, IRS assesses the tax. With an assessment notice, IRS formally notifies the taxpayer that the specified amount of tax is owed and that interest and penalties may accrue if the tax is not paid by a certain date. The assessed amount, not the amount an auditor recommends at the end of the audit, establishes the taxpayer's liability.

If the taxpayer disagrees with an examination's recommendation, the recommendation may be protested to IRS' Office of Appeals or the dispute can be taken to court.[24] The Office of Appeals settles most of these

[24]Taxpayers may appeal to Tax Court without paying the tax or pay the tax and claim a refund in the U.S. Court of Federal Claims or a federal district court.

disputes, and the remainder are docketed for trial. Agreements made in settlements and court decisions determine the assessed part of the disputed tax.

The issue of reductions in recommended tax was raised in the Committee's hearing by IRS auditors who alleged that some supervisors "zeroed out" or reduced the results of audits—that is, the audits were closed with no or reduced recommended additional tax, without a basis in law or IRS procedure. The witnesses further alleged that the reasons for zeroing out included retaliating against auditors to diminish their chances for promotion, favoring former IRS employees in private practice, and exchanging zeroing out for bribes and gratuities from taxpayers.[25]

Data Collected by IRS

IRS has not systematically collected data on the extent to which additional taxes recommended by auditors have been zeroed out or reduced without a basis in law or IRS procedure. In particular, IRS had no data on supervisors' improperly limiting auditors' recommendations of additional tax before an audit was closed. However, IRS collects data on the amounts of recommended taxes that were not assessed and the number of examinations closed with no change in tax liability.

One of our recent reports illustrates the lack of data on the extent to which supervisors improperly limit auditors' recommendations of additional tax.[26] We found that an estimated 94 percent of IRS workpapers lacked documentation that the group manager reviewed either the support for adjustments or the report communicating the adjustments to the taxpayer. IRS managers acknowledged that because of competing priorities, they could not thoroughly review workpapers for all audits. IRS officials commented that supervisory reviews were usually completed through other processes, such as reviewing time spent on an audit, conducting on-the-job visits, and discussing cases with auditors. We recommended that the IRS Commissioner require all audit supervisors to document their review of all workpapers to help ensure the quality of all examinations.

In another recent report, we found that most additional taxes recommended by IRS auditors were not assessed. Table 10 shows taxes recommended by IRS auditors and the percentage of these amounts assessed for audits closed in fiscal years 1992 through 1997. During these

[25]Further information on these issues is in GAO/OSI-99-9R.

[26]IRS Audits: Workpapers Lack Documentation of Supervisory Review (GAO/GGD-98-98, Apr. 15, 1998).

years, at most, 41 percent of the additional taxes recommended during audits were assessed.

Table 10: Status of Additional Amounts Recommended for Individual, Corporate, and Other Audits Closed in Fiscal Years 1992-97, as of September 27, 1997

Dollars in billions

Fiscal year	Recommended amount	Percentage assessed
1992	$24.8	34
1993	22.0	40
1994	22.6	41
1995	27.2	40
1996	30.8	36
1997	31.7	38

Note: Dollars are in current dollars.

Source: Tax Administration: IRS Measures Could Provide a More Balanced Picture of Audit Results and Costs (GAO/GGD-98-128, June 23, 1998).

Other IRS data showed that many examinations were concluded with no recommended additional tax. For example, according to IRS' Fiscal Year 1997 Data Book, 24 percent of the corporate examinations completed during fiscal year 1997 were closed with no proposed tax change.

Reasons for Reducing Recommended Tax

Our previous work identified several factors that, in part, explained why recommended additional taxes were not assessed after audits were closed.[27] Factors like these could also explain some actions by supervisors to zero out or reduce recommended tax amounts prior to audits being closed. However, IRS does not collect data on the extent to which these factors, or others, contribute to supervisors' decisions prior to audits being closed.

We reported that the complexity and vagueness of the tax code was one explanation for recommended taxes not being assessed after a corporate audit was closed. Because of the complexity and vagueness of the tax code, IRS revenue agents had to spend many audit hours to find the necessary evidence to clearly support any additional recommended taxes. In addition, differing interpretations in applying the tax code to underlying transactions increased the likelihood of tax disputes. Because corporate representatives usually prevailed in Appeals or the courts, additional taxes recommended were often not actually assessed.

We also reported that aspects of the corporate audit process for large corporations also made it difficult for revenue agents to develop enough support to recommend tax changes that could survive a taxpayer appeal.

[27] Tax Administration: Factors Affecting Results From Audits of Large Corporations (GAO/GGD-97-62, Apr. 17, 1997).

For example, revenue agents worked alone on complex, large corporation audits with little direct assistance from district counsel or their group managers. In addition, when selecting returns for audit, the agents had little information on previously audited corporations or industry issues to serve as guideposts. Finally, the agents had difficulty obtaining relevant information from large corporations in a timely manner.

IRS Internal Audit[28] recently cited several factors that contributed to low productivity, as partially manifested by high no-change rates, in the Manhattan District Office. IRS acknowledged that in 1995, it took aggressive action to close old examinations. Also, audit group managers in Manhattan and two other districts did not have enough time to perform workload reviews to ensure quality examinations. Manhattan was below the IRS regional average in complying with IRS audit standards for such things as depth of examinations and workpaper support for conclusions.

We also reported that relying too heavily on additional taxes recommended as a measure of audit results might create undesirable incentives for auditors. We found that audits of large corporations raised concerns that relying on recommended taxes as a performance indicator might encourage auditors to recommend taxes that would be unlikely to withstand taxpayer challenges and thus not be assessed.[29] Supervisors on guard against this incentive, which might have also influenced them, might have been accused of improper zeroing out. In this connection, we recently reported that IRS examination and collection employees perceived that managers considered enforcement results when preparing annual performance evaluations.[30]

IRS is increasing its efforts to ensure that enforcement statistics are not used to evaluate its employees. In commenting on our report on enforcement statistics, the Commissioner stated that IRS was taking several actions to ensure that all employees comply with its policies on the proper use of enforcement statistics. These actions included redrafting applicable sections of the Internal Revenue Manual, establishing a panel responsible for answering all questions IRS received on enforcement statistics, and establishing an independent review panel to monitor compliance with restrictions on using enforcement statistics. In addition,

[28] Productivity of the General Examination Program in the Manhattan District, IRS Internal Audit Report, Reference No. 680904, Jan. 30, 1998.

[29] GAO/GGD-98-128.

[30] IRS Personnel Administration: Use of Enforcement Statistics in Employee Evaluations (GAO/GGD-99-11, Nov. 30, 1998).

in January 1999, IRS proposed establishing a balanced system of organizational measures focusing on quality and production measures, but not including tax enforcement results.

Witness Allegations of Improper Zeroing Out

Several of the individual allegations made by IRS employees that we reviewed involved the issue of improper zeroing out of additional taxes by IRS managers. The eight specific cases in question involved large organizations, and the issues generally related to complex financial transactions.

We found no evidence to support the allegations that IRS managers' decisions to zero out or reduce proposed additional taxes were improper. Instead, we found that the managers acted within their discretion and openly discussed relevant issues with involved IRS agents, technical advisors, and senior management. Ultimately, the decisions were approved by appropriate individuals and were documented in the files.

Several of the cases demonstrated some of the concerns and issues we have raised in our prior work concerning audits of large corporations. For example, the complexity and vagueness of the tax code create legitimate differences in interpretation and administering the tax system creates a tension in seeking a proper balance between the tax administrator's need for supporting documentation and the taxpayer's burden in providing such information.

Equal Employment Opportunity Issues in IRS' Midwest District Office

IRS has acknowledged problems related to the EEO climate in its Milwaukee, WI, area offices and over the last few years has moved to address them. After a finding of discrimination in 1995 in the case of one employee, a new district director initiated an internal review, and, afterwards, IRS appointed an outside review team to study the EEO situation. The internal study made 53 recommendations in broad categories related to creating a supportive work culture, understanding issues, preparing employees for promotion, and examining the promotion process. The outside study found no discriminatory hiring or promotion practices, but it did make recommendations related to hiring and promotions, among other things.

Background

Problems with the EEO climate in IRS' Midwest District Office, which is headquartered in Milwaukee, date back several years. In 1995, Treasury agreed with an Equal Employment Opportunity Commission administrative judge who found that a district employee was the victim of discrimination and retaliation. Also, Wisconsin congressional offices received EEO-related complaints from IRS employees, and internal and

external groups were critical of district EEO matters. According to the District Director who arrived in early 1996, the district was perceived to run on "good-old-boy" connections. Also, the district, which was created in 1996 through the merger of three smaller districts, was facing possible layoffs, further contributing to tense labor-management relations.

Two Studies of the EEO Climate Made Numerous Recommendations

To try to better identify some of the underlying causes of the problems in IRS Milwaukee area offices, the District Director commissioned an IRS team in April 1996 to assess the EEO climate and make recommendations for corrective action. As part of its review, the team distributed a survey to all Milwaukee area district employees to gather EEO-related perceptions.

On the basis of its review of the survey results and other data, in December 1997, the team reported that a lack of trust and goodwill pervaded the work environment. The survey revealed that people in all groups (e.g., males, females, nonminority whites, African Americans, and Hispanics) believed they were less likely than people in other groups to receive promotions, significant work assignments, training opportunities, and formal recognition or rewards. Specific problems cited in the report included little recent diversity training, a belief by certain minority employees that stereotypes negatively affected their treatment, difficulties in widely disseminating information, gaps in EEO communication, no formal mentoring program, and much dissatisfaction with how employees were selected for promotion.

On the basis of its findings, the assessment team made 53 recommendations in 4 categories. The categories covered creating a supportive culture, creating a greater understanding of issues, preparing employees for promotion, and examining ways that employees were selected for promotion. In a 5th category—examining the representation of minorities in the district—the team made 21 more recommendations that were expected to be suspended pending an IRS analysis of the ramifications of certain court cases.

The District Director who commissioned the climate assessment report praised it and the process that produced it. During his tenure, many actions were taken to address the district's EEO problems. For example, (1) policy statements were issued tolerating no discriminatory behavior, (2) minority representation in the Director's and EEO offices was increased, (3) the EEO office was given more privacy, (4) baselines were set to measure the impact of any improved hiring or promotion policies, (5) minorities were promoted to positions of authority, and (6) training was provided. Goals were also set to open communications with

employees, employee and community groups, and the media; treat individual performance cases fairly; and not debate emotionally charged personnel issues in the press.

In spite of the climate assessment team's efforts and the various changes made or planned, the district's EEO problems persisted. Consequently, IRS and certain members of the Wisconsin congressional delegation agreed that another team should independently review the situation.[31]

To try to preserve its independence, the team purposefully had no representation from IRS. Also for this reason, it solicited no IRS comments on its draft report.

The team interviewed more than 100 people and examined over 130 records and files, although it did not scientifically select interviewees or broadly survey all district employees. Team members told us they tried to ensure broad coverage by talking to many people and to all sides of general issues. Moreover, they relied on the climate assessment survey to summarize perceptions. They also, however, relied extensively on anecdotal information without determining its objectivity or accuracy.

In August 1998, the team reported, among other things, that (1) many employees had no confidence in the EEO process and feared retaliation if they filed complaints or participated in a way considered adversarial to management, (2) separating EEO functions into outreach and traditional EEO/counseling components was not working effectively, (3) the counseling program was in disarray, and (4) confusion existed over the role of Treasury's Regional Complaint Center in the formal EEO complaint process. Also, although anecdotes collected by the team did not support a sweeping indictment of Milwaukee IRS management practices, the report concluded that, intentionally or not, some practices perpetuated a work environment that was historically insensitive to the concerns of female and minority employees.

On the basis of its review, the team made recommendations in different areas. For instance, many recommendations dealt with the team's findings related to the district's EEO process for resolving issues in a precomplaint stage and its relationship to Treasury's formal complaint process. The team also made recommendations relating to hiring and promotions in spite of finding no discriminatory pattern or practice in promoting or

[31]Members of the congressional delegation were Senators Russell Feingold and Herb Kohl and Representatives Tom Barrett and Gerald Kleczka.

hiring minorities or women. The report noted that African Americans in IRS' Milwaukee and Waukesha, WI, offices appeared underrepresented when compared to the Milwaukee civilian labor force.[32]

Although district managers and representatives of employee groups disagreed with many of the issues and assertions in the report, there was general agreement with many of the recommendations. For instance, the head of the diversity office at the time of the study informed us that he agreed with the substance of, had actually taken action related to, or would favor forwarding to Treasury many of the report's recommendations.

After the report was released, IRS initiated several significant actions to address problems identified. Chief among these was appointing a new District Director who arrived in the district in mid-November 1998 with a stated commitment to overcome past problems. In that regard, she described to us her intent to open communication channels and deal with disrespect, nastiness, and mean-spiritedness at all levels. She emphasized her themes of communication, responsibility, and accountability and told us that on her second day in the district she discussed these themes at an off-site meeting with top managers and union, EEO, and diversity officials.

The new District Director also expressed to us her commitment to work with various interest groups. In addition, she combined the district's EEO and diversity functions, made EEO positions permanent as opposed to rotational, and invited a union representative to be present for interviews for a new EEO officer.

The new District Director stated that these actions were on the right track, but because of the long and contentious history of EEO problems in the district, improvements and success will take time. She also noted that better communication and cooperation among IRS and the various internal and external stakeholders will be extremely important in dealing with the district's long-standing problems.

Agency Comments

In commenting on a draft of this report, the Commissioner of Internal Revenue described IRS actions on the issues we noted. For instance, he shared our concern that IRS needed to improve how it managed executive misconduct cases. He noted that the recently created Commissioner's

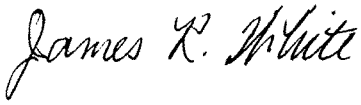
[32]The head of the study team acknowledged that the proper statistical comparison was with the local qualified labor force, not the civilian labor force. However, according to another study team member, the relevant qualified labor force statistics were not available.

Complaint Processing and Analysis Group, proposed as the Commissioner's Review Group, will coordinate IRS' efforts to improve complaint information, especially relating to alleged reprisal against whistleblowers, so that complaints will be promptly and fairly resolved. IRS will also share more information with employees and the public on responses to reprisals and other complaints to highlight a message that all employees will be held accountable for their actions. The full text of the Commissioner's comments is reprinted in appendix IV.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of this letter. At that time, we will send copies to Senator Daniel Patrick Moynihan, the Ranking Minority Member of the Senate Committee on Finance; the Honorable Charles O. Rossotti, Commissioner of Internal Revenue; other interested congressional committees; and other interested parties.

This work was done under the direction of Joseph E. Jozefczyk, Assistant Director for Tax Policy and Administration Issues. Other major contributors are listed in appendix V. If you have questions, you may contact me on (202) 512-9110.

Sincerely yours,



James R. White
Director, Tax Policy
and Administration Issues

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Abbreviations

ALERTS	Automated Labor and Employee Relations Tracking System
CWA	closed without action
DO	deciding official
EEO	equal employment opportunity
GS	general schedule
IRS	Internal Revenue Service
MSPB	Merit Systems Protection Board
OES	Office of Executive Support
OIG	Office of Inspector General
OLR	Office of Labor Relations
OSC	Office of Special Counsel
RO	recommending official
SES	Senior Executive Service
TIGTA	Treasury Inspector General for Tax Administration

Objectives, Scope, and Methodology

We organized our work to bring together information bearing on the five issues contained in your May 21, 1998, request letter. Accordingly, our objectives were to

(1) determine if senior Internal Revenue Service (IRS) managers received the same level of disciplinary action as line staff;

(2) determine to what extent, if any, the IRS Deputy Commissioner might have delayed action on substantiated cases of employee misconduct until senior managers were eligible to retire;

(3) ascertain the extent to which IRS employees might have retaliated against whistleblowers and against taxpayers or their representatives who were perceived as uncooperative;

(4) determine the extent to which IRS employees might have zeroed out or reduced the additional tax recommended from examinations for reasons not related to the merits of the examinations; and

(5) describe equal employment opportunity (EEO) issues in IRS offices in the Milwaukee metropolitan area.

Our scope and methodology related to each of these objectives follow.

Disciplinary Actions for Senior Executive Service and Lower-Level Staff

To compare disciplinary experiences of Senior Executive Service (SES) and lower-level employees, we matched data accumulated by sampling senior executives' misconduct cases against data for lower-level employees extracted from IRS' broader disciplinary database, the Automated Labor and Employee Relations Tracking System (ALERTS). We compiled general statistics on how long senior executive cases took by collecting information from every second nontax SES case file in IRS' Office of Executive Support (OES) that was active sometime between January 1, 1996, and June 30, 1998.[1] Our sample included 70 cases.

For each case in our sample, we extracted and recorded data from the relevant case file. These data included issues involved, processing dates, information on whether allegations were substantiated by investigators, disciplinary actions proposed and adopted, and information related to retirement.

[1]We excluded cases related to employees' tax compliance because they were different in nature from the cases raised at the April 1998 Senate Finance Committee hearings.

For lower-level employees, that is, general schedule (GS) employees, we obtained selected parts of the ALERTS database from IRS. We ran our statistical analyses on ALERTS cases that IRS' Office of Labor Relations received between January 1, 1996, and June 30, 1998, and on cases that were closed within that period. More specifically, we focused on administrative and IRS Inspection Service cases within ALERTS because they were the categories in which conduct matters were found. Although we did not audit ALERTS, IRS officials told us that this data system had over the years had flaws, but they also told us it was better than it used to be. Because ALERTS was the only source of information available on lower-level disciplinary actions, we used it to the extent that it had information comparable to what we collected on senior-level cases.

We also reviewed recent internal IRS and independent studies of IRS' disciplinary systems and interviewed IRS officials about their plans for revamping the systems. One IRS study we reviewed used the lower-level disciplinary database to assess the effect of IRS' using a guide to determine appropriate disciplinary action. We also became familiar with the Douglas Factors, shown in appendix II, governing disciplinary actions imposed and asked IRS officials about the differences, if any, they perceived between SES and lower-level cases.

Alleged Delays by IRS Deputy Commissioner on SES Misconduct Cases

We examined the question of alleged delays in dealing with cases of alleged misconduct by senior executives by taking several steps. First, we studied in depth the five specific cases mentioned in the April 1998 hearings. This involved examining investigative and personnel files as well as files maintained by OES. In addition, we interviewed various IRS officials, including the Deputy Commissioner, about these cases.

In addition, we used the 70-case sample of senior executive cases previously described to obtain more broad-based information about any possible delays. Although most of our analyses were based on this sample, to learn more about the cases that took the most time, we also examined every case file IRS could find that appeared on lists of cases awaiting action at OES for at least 90 days during the January 1, 1996, through June 30, 1998, period we were studying. We also examined cases that appeared on logs that IRS kept so we could better ensure we were not overlooking cases we did not otherwise encounter for the period. In all, we examined the 70 cases in our sample plus 43 more cases on lists and logs for a total of 113 cases. Because some individuals were involved in more than 1 case, the 113 cases we analyzed covered 83 senior executives. We extracted the same type of information from each of the case files that we extracted

from the sampled case files. Examining lists, logs, and files allowed us to see if recordkeeping practices might have contributed to any delays.

To examine the relationship between case-processing and retirement dates, we analyzed where in the case-processing sequence the retirement dates provided us by OES fell. In instances in which OES was also able to readily provide retirement eligibility dates, we considered them in examining processing timeliness as well.

Number of Whistleblowing Reprisal Cases and Extent of Information on IRS Retaliation Against Taxpayers

To tabulate the number of whistleblowing reprisal cases, we obtained information from the Office of Special Counsel (OSC) and the Merit Systems Protection Board (MSPB). We did this for the number of cases involving IRS employees, and for contextual purposes, for cases from throughout the federal government.

For governmentwide data, we used either information already published or data generated specifically for us. For IRS data, the agencies did special searches of their databases. We did not audit the OSC or MSPB data systems. Because in the MSPB data system not all IRS cases could be isolated, we examined actual case rulings that MSPB gathered for us or that we located on the Internet, looking for Department of the Treasury cases that were really IRS cases. For Treasury cases for which MSPB was not able to give us timely information and information was not on the Internet, we asked IRS to identify whether they involved IRS employees.

In looking for information on IRS employees who might have retaliated against taxpayers or their representatives who were perceived to be uncooperative, we studied our reports on taxpayer abuse. In addition, we interviewed IRS officials and investigated entries under specific codes in various databases to see if relevant issues appeared. Finally, we discussed with IRS officials changes to the information systems that might be coming in the future.

Alleged Improper Zeroing Out or Reduction of Recommended Tax

Concerning information on the improper zeroing out or reduction of additional tax recommended, we studied our and Inspection Service reports dealing with examination issues related to audit results. We specifically considered our and IRS information on the extent to which IRS audit recommendations were actually assessed and the factors that could explain the results.

EEO Issues in IRS' Midwest District Office

To describe EEO issues in the Milwaukee area, we examined the report of an outside team studying the program and the documents that the team accumulated in doing its work, including an IRS internal EEO climate

assessment study. We also interviewed key study participants and affected parties in Washington, D.C., and Milwaukee to better understand what the EEO climate in the area was, how the study report was done, and what had happened since the report was finished.

In addition to addressing the concerns of the Senate Committee on Finance, we planned our work to respond to a mandate in the Conference Report on the IRS Restructuring and Reform Act of 1998. The conferees intended for us to review the study team report.

We did our work in Washington, D.C., and Milwaukee between June 1998 and March 1999 in accordance with generally accepted government auditing standards.

The Douglas Factors

The Douglas Factors are as follows:[1]

- The nature and seriousness of the offense, and its relation to the employee's duties, position, and responsibilities, including whether the offense was intentional or technical or inadvertent, or was committed maliciously or for gain, or was frequently repeated;
- the employee's job level and type of employment, including supervisory or fiduciary role, contacts with the public, and prominence of the position;
- the employee's past disciplinary record;
- the employee's past work record, including length of service, performance on the job, ability to get along with fellow workers, and dependability;
- the effect of the offense upon the employee's ability to perform at a satisfactory level and its effect upon supervisors' confidence in the employee's ability to perform assigned duties;
- consistency of penalty with those imposed upon other employees for the same or similar offenses;
- consistency of the penalty with the applicable agency table of penalties;
- the notoriety of the offense or its impact on the reputation of the agency;
- the clarity with which the employee was on notice of any rules that were violated in committing the offense, or had been warned about the conduct in question;
- potential for employee's rehabilitation;
- mitigating circumstances surrounding the offense such as unusual job tensions, personality problems, mental impairment, harassment, or bad faith, malice or provocation on the part of others involved in the matter; and
- the adequacy and effectiveness of alternative sanctions to deter such conduct in the future by the employee or others.

[1]Douglas v. Veterans Administration, 5 M.S.P.R. 280 (1981).

Summaries of Alleged Senior-Level Misconduct Cases

This appendix summarizes information about the five senior-level misconduct allegations cited in the April 1998 Senate Finance Committee hearings. The summaries include information about when the executives were eligible to retire and about whether their eligibility dates might have related to how their cases were processed. We refer to the executives in these five cases as Executives A through E.

Executive A Allegations

An IRS employee filed a complaint that Executive A and two other IRS employees violated IRS ethics rules. The IRS employee also alleged that Executive A and the two other employees retaliated against her for reporting the ethics violations. The alleged violations included manipulating a rating system, giving an improper award, falsifying records, and not reporting time card fraud, although Executive A was only alleged to be involved in the last violation. Treasury's Office of Inspector General (OIG) did not find that Executive A was culpable for ethics violations but found that the other two employees were culpable. IRS attorneys reviewing the case concluded that the information in the OIG report did not demonstrate misconduct on Executive A's part.

Executive A was not eligible for retirement when the allegation was made or when the OIG investigation was closed.

Executive B Allegations

This case started when the OIG received an anonymous allegation that Executive B abused travel authority.[1] IRS officials reviewed the allegation and found that Executive B had authorized unjustified travel expenditures. Local management then counseled Executive B that all expenditures needed to be authorized according to IRS procedures. This counseling was confirmed in writing. However, contrary to IRS policy, the counseling took place before the Deputy Commissioner concurred with the proposed case resolution.

Executive B was already eligible for retirement at the time the allegation was made.

Executive C Allegations

The OIG received an anonymous complaint that Executive C was abusing official travel. The OIG report concluded that Executive C made personal use of some travel benefits earned on government travel.

The offices considering the case disagreed among themselves over the facts, the adequacy of the investigation, and the steps to be taken next. The

[1]The allegation included two other issues that were immediately closed because they had been previously reviewed.

Director of IRS' Human Resources Division, which was involved in executive misconduct cases earlier in the 1990s, advocated a reprimand, but the recommending official thought that significant circumstances mitigated any disciplinary action. OES prepared a statement of differences and recommended a reprimand.[2] A few months later, the recommending official, finding no abuse and unclear IRS guidance in the area, recommended closing the case without action but cautioning the executive. The next month, the OES official who previously recommended a reprimand sent the case to the Deputy Commissioner, this time agreeing with the recommending official's position. A few months after that, the OIG reminded the Deputy Commissioner of the previous year's report and requested appropriate action. Later, OIG officials told OES that they disagreed with OES' recommendation to close the case without action. Finally, OES wrote the Deputy Commissioner reaffirming the recommendation for closure without action but with cautioning.

The Deputy Commissioner counseled the executive 5-½ years after the case began and 18 months after receiving the case. When we asked the Deputy Commissioner why the final stage of case processing took so long, he had no explanation.

Executive C was not eligible for retirement at the time the allegation was made or at the time he was counseled.

Executive D Allegations

The IRS sexual harassment hotline received an anonymous allegation that Executive D might have harassed a staff member. During the Inspection Service investigation, Executive D refused to answer a question he believed was irrelevant. In its report, the Inspection Service summarized the facts of the investigation and did not conclude whether there was a violation of IRS ethical standards.

OES and the recommending official disagreed in their analyses of the report and their resulting recommendations. OES concluded that a 15-day suspension was warranted for the refusal to answer a question even though IRS counsel was not sure a violation really occurred. OES also raised the possibility of reassigning Executive D. The recommending official believed that, in this case, refusal to answer a question did not violate ethics rules, but that counseling was warranted.

[2]OES was previously known as the Office of Ethics and Business Conduct, but in this section only the designation OES will be used.

About 39 months after OES prepared a statement of differences, an Inspection Service case-tracking entry indicated that IRS management planned no action on the case. The next year, OES closed the case "administratively" due to the employee's retirement.

The Deputy Commissioner told us that, several years before its administrative close, the case was "de facto closed" with Executive D's transfer. He stated that the transfer was the appropriate disciplinary action because Executive D was too familiar with local employees.

OES did not close the case until the individual retired several years after the transfer. It did not realize that the Deputy Commissioner considered it closed earlier. Also, IRS officials we asked could not find the case file for at least a few months.

Executive D was eligible for retirement at the time the allegation was made.

Executive E Allegations

The Inspection Service began an investigation after an anonymous caller reported to Internal Security that Executive E abused her authority. More than a year later, the investigation confirmed the allegation, and the Director of the Human Resources Division recommended that a letter of reprimand be issued. More than 4 years after that, OES recommended sending a letter of reprimand or a letter confirming counseling. The Deputy Commissioner sent Executive E a letter of counseling 5-½ years after the original complaint and more than 4 years after receiving the case.

The Deputy Commissioner explained to us that he had not been comfortable with the allegations' correctness, but that he eventually agreed that the allegations had some merit. He added that the delay in closing the case occurred because he allowed the case to be lost in the system. He did not, he said, cover up for Executive E. Specifically, he stated that reduced OES staffing and a poor information system were contributing factors to the case being delayed without a disposition.

Executive E was not eligible for retirement at the time the allegation was made or at the time the counseling letter was sent.

Comments From the Internal Revenue Service

COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

May 13, 1999

Ms. Nancy Kingsbury
Acting Assistant Comptroller General,
General Government Division
U.S. General Accounting Office
441 G Street, NW
Washington, D.C. 20548

Dear Ms. Kingsbury:

Thank you for the opportunity to review and comment on your draft report titled Tax Administration: Allegations of Internal Revenue Service Employee Misconduct. The issues raised in the report are important to the credibility of the Internal Revenue Service (IRS) and the confidence of the public and our employees. We are committed to improving the IRS through our goals of service to each taxpayer, service to all taxpayers, and productivity through a quality work environment.

I share your concern that the IRS management of executive misconduct cases needs substantial improvement. I also appreciate your recognition of the steps we are taking to make these improvements. The recent creation of the Commissioner's Complaint Processing and Analysis Group represents a significant commitment of resources and attention to complaint intake, fact-finding, and adjudication of cases where allegations of misconduct are substantiated. This group will also coordinate our efforts to improve the quality of information on complaints, especially those involving allegations of reprisal against whistleblowers. This information will help us ensure prompt and fair resolution of complaints and use complaints as a source of strategic information to improve the integrity of Service operations.

Statistical reporting requirements included in the IRS Restructuring and Reform Act address the specific concern you raised about the lack of data on reprisal. We will share this and other information on actions taken in response to complaints with IRS employees and the public, including summaries of specific cases. This will reinforce the message that everyone, regardless of position, will be held accountable for their actions. I saw the benefits of this approach when we publicized the actions taken based on the work of the special panel of senior career civil servants from other federal agencies who reviewed the misuse of enforcement statistics at the national level. I am taking a similar approach in publicizing the actions we are taking to address the issue of misuse of statistics and improper seizures at regional and district offices. I have asked the National Director of the Commissioner's Complaint Processing and Analysis Group to develop a semiannual report that will continue this policy. As you know, I have taken

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a strong stand on the issue of retaliation against IRS employees who come forward with information about wrongdoing. I have made it clear to all IRS employees through numerous memoranda, policy statements and all-employees messages that retaliation is intolerable, and that I will take decisive action in any case where retaliation is found to have occurred. In keeping with this commitment, our May 11, 1999, Mid-Year Business Meeting featured a presentation from the Office of Special Counsel to all of our executives on their obligations under the Whistleblower Protection Act.

Allegations of improper adjustments in tax assessments or of retaliation against taxpayers and their representatives who assert their rights are even more troublesome for the IRS, as they strike to the core of our responsibility to fairly administer the revenue laws. Thus, I was relieved that you found no evidence of improper adjustments to taxes and that managers acted properly in making adjustments to tax assessments. Similarly, your findings that there was no evidence of vendettas by criminal investigators against taxpayers, that decisions to initiate investigations were reasonably based on information available to IRS at the time, and that there was no evidence of impropriety in obtaining and executing search warrants, will be helpful as we move to implement the recommendations of Judge Webster's recent report for improving the Criminal Investigations Division.

In the important and difficult process of changing the IRS to deliver on our mission, it is essential to address carefully every serious allegation of wrongdoing to arrive at our best understanding of the facts and to act accordingly to improve for the future. I believe your report has aided in this endeavor.

If you have any further questions please call me at (202) 622-9511 or Stephen Whitlock, National Director of the Commissioner's Complaint Process and Analysis Group, at (202) 622-6383.

Sincerely,

Charles O. Rossotti

Charles O. Rossotti

Appendix V

Major Contributors to This Report

General Government Division, Washington, D.C.

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Leon H. Green, Senior Evaluator
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GAO Report on Allegations of IRS Taxpayer Abuse

A GAO report (GAO/OSI-99-9R), released in redacted form under FOIA, says the office found no evidence of IRS managers' improper decisions on tax assessments and of IRS retaliations against specific taxpayers during criminal investigations.

Citations: GAO/OSI-99-9R (redacted)

Date: May 24, 1999

========== SUMMARY ==========

A General Accounting Office report (GAO/OSI-99-9R), released in redacted form under the Freedom of Information Act, says the office found no evidence of IRS managers' improper decisions on tax assessments and of IRS retaliations against specific taxpayers during criminal investigations.

========== FULL TEXT ==========

UNITED STATES GENERAL ACCOUNTING OFFICE

OFFICE OF SPECIAL INVESTIGATIONS

SPECIAL REPORT

RELEASED UNDER THE FREEDOM OF INFORMATION ACT
FOIA

RESTRICTED

B-282324

May 24, 1999

The Honorable William V. Roth, Jr.
Chairman
Committee on Finance
United States Senate

Subject: Tax Administration: Investigation of Allegations of Taxpayer Abuse and Employee Misconduct Raised at Senate Finance Committee's IRS Oversight Hearings

Dear Mr. Chairman:

[1] This letter contains the results of our investigation into allegations of taxpayer abuse and employee misconduct that were made during the April 1998 Internal Revenue Service (IRS) oversight hearings held by your Committee. You asked us to investigate the specific allegations, determine if additional action is needed, and identify any underlying systemic or programmatic problems that need to be resolved to protect the rights of taxpayers and IRS employees. In discussions with your office, we agreed to investigate specific allegations that (1) IRS employees have closed audits with no change in tax liability or with a complete (zeroed-out) or partial reduction in proposed assessments for reasons unrelated to the merits of the cases and (2) IRS has retaliated against taxpayers and their representatives who have been perceived to be noncooperative. The systemic issues raised in your request are being addressed by GAO's General Government Division and will be reported separately. [1]

RESULTS IN BRIEF

[2] Based on our investigation, we did not find any evidence to support the allegation that IRS managers' decisions to "no-change" or "zero-out" proposed tax assessments were improper. The witnesses were correct in some of the facts supporting their allegations in some of the cases. However, our investigation established that the allegations themselves had been based on an incomplete awareness of the total circumstances surrounding the matters. We found that each manager had acted within his or her discretion and openly discussed relevant issues with both the employee and senior management. Their decisions were approved by appropriate individuals and were documented in the files. These managers followed IRS policies and procedures related to auditing taxpayers. However several of these cases are illustrative of concerns raised in our prior work. [2] We previously reported that (1) the complexity and vagueness of the tax code cause differences in interpretation and (2) the tax system creates a tension in seeking a proper balance between the tax administrator's need for information and the taxpayer's burden in providing information. These factors, among others, contributed to the high rate of audits that were closed with no changes in taxes owed.

[3] Generally, we found no corroborating evidence that the criminal investigations described at the hearing were retaliatory against the specific taxpayer. In addition, we could not independently substantiate that IRS employees had vendettas against these taxpayers. Our investigation did find that decisions to initiate the investigations were reasonably based on the information available to IRS at the time and were documented in agency files when they were made. Further, we found no evidence that IRS employees had acted improperly in obtaining and executing the search warrants. However, in one case, we were denied access to key witnesses, due to civil litigation. As a result, we were unable to express any opinion in connection with this case.

MANAGERS ZEROING-OUT OR NO-CHANGING TAX ASSESSMENTS

[4] During the hearing, a panel of four current IRS employees [3] testified about a number of concerns, they had about managers using their discretion to improperly zero-out or no-change the tax liabilities of large taxpayers. These decisions were allegedly made to improve statistics, gain personal awards, or pursue careers outside the IRS. Some of

these witnesses also alleged that former IRS managers were representing taxpayers before the IRS and, because of their prior relationships, influencing audits. While conducting this investigation, we identified another IRS employee [4] with similar allegations and cases that allegedly supported his position. The witnesses also made specific allegations regarding the inappropriate conduct of certain IRS managers. We have included the results of our investigation into these allegations.

[5] A synopsis of the allegations raised by each witness follows. A more detailed discussion of the allegations and our investigative findings is included in enclosures I through V.

[6] Ginger Jarvis is a revenue agent with the Coordinated Examination Program (CEP) [5] in the Manhattan District Office. She alleged in her testimony that millions- perhaps hundreds of millions -- of dollars of tax revenues owed to the U.S. Treasury by some of the largest taxpayers in this country are "literally forgiven, or zeroed-out," at the sole discretion of individual managers. She added that these decisions are based on certain managers' desire (1) to improve statistics to gain status and personal awards or (2) to obtain careers outside IRS. To support her assertion, Ms. Jarvis provided case examples. Ms. Jarvis's specific allegations and our investigative findings are included in enclosure I.

[7] Michael Ayala is an analyst in the Southeast Regional Office, Atlanta, Georgia. During his testimony, he stated that he had witnessed a broad range of misconduct by senior managers in both tax administration and civil service practices. This misconduct allegedly included mistreatment of taxpayers, covering up serious revenue losses and misconduct by senior managers, and improper use of enforcement statistics. Mr. Ayala provided specific examples to support his allegations. Mr. Ayala's specific allegations and our investigative findings are included in enclosure II.

[8] Maureen O'Dwyer is an examiner with the International Enforcement Program (IEP) [6] in the Manhattan District Office. She testified that she believes that some managers enforce the Internal Revenue code and regulations unevenly and provided specific case examples. Ms. O'Dwyer's specific allegations and our investigative findings are included in enclosure III.

[9] Minh Thi Johnson is a revenue agent in the Los Angeles District Office. She provided testimony concerning what she considered to be abuses by IRS employees and cited several examples. Ms. Johnson's specific allegations and the results of our investigation are included in enclosure IV.

[10] During our investigation of the allegations raised by Ms. O'Dwyer, we met with * * *, an examiner with IEP in the Manhattan District Office. * * * believes employees in the International Examination Branch are working in an atmosphere of fear. He stated that former IRS managers who now work for major accounting firms were using their former associations with current managers to influence audits. * * * provided two specific examples. * * * allegations and the results of our investigation are included in enclosure V.

PREVIOUS GAO FINDINGS

[11] We previously reported on a review of large case audits, including CEP audits. [7] Among the concerns raised in these reports were factors that contributed to the high rate of audits that had been closed with no tax changes. Two of these factors were the following: (1) The complexity and ambiguity of the tax code cause differences in interpretation; and (2) the tax system creates a tension in seeking a proper balance between the tax administrator's need for information and the taxpayer's burden in providing information.

[12] The complexity and vagueness of the tax law make it difficult for IRS auditors to clearly support a recommendation for any additional tax. Without clear tax laws, resolution of disputes can be complicated and can ultimately depend on the negotiating skills of the IRS and corporate representatives. A major reason for disputing recommended taxes was disagreement by the taxpayer with a revenue agent's interpretation of tax laws. Moreover, in our investigation we found that IRS employees and IRS management disagreed on how to interpret the application of the law. For example, Ms. Jarvis and IRS management disagreed about interpretations of the tax laws regarding the * * *. (See enclosure I.)

[13] We also found instances where the CEP audit team's legitimate needs for taxpayer-provided information were not met. CEP teams and corporations may disagree about the types and amount of information needed for an audit, thus causing a tension between IRS and the taxpayer. This appears to have been a contributing factor in one case described by Ms. Jarvis (see enclosure I) and in the two cases mentioned (see enclosure V).

RETALIATION BY IRS IN CONDUCTING CRIMINAL INVESTIGATIONS

[14] At the hearing, a panel of four taxpayers [8] testified about their concerns that IRS's Criminal Investigation Division (CID) improperly selected them for investigation based on information from unreliable sources and/or a personal vendetta. Three of the witnesses believed that IRS should have used subpoenas instead of search warrants. Further, there were allegations of misconduct on the part of IRS agents who executed the search warrants. A synopsis of the allegations raised by each witness follows. A more detailed description of the allegations with our investigative findings is included in enclosures VI through IX.

[15] William Moncrief is the president of Montex Drilling Company, a family-owned company that is involved in oil and gas development. Its headquarters is located in Fort Worth, Texas. CID conducted a criminal investigation of Mr. Moncrief, Montex, and other related entities. Mr. Moncrief alleged that IRS should have conducted a civil audit instead of a criminal investigation and that IRS continued the criminal case as a means to extort a settlement. He also stated that the government had used a search warrant instead of a subpoena and complained about abuses by IRS agents in executing the search warrant. Mr. Moncrief's specific allegations and the results of our investigation are included in enclosure VI.

[16] John Colaprete is part owner of Mom's, Inc., which operated The Jewish Mother restaurants in Virginia Beach and Norfolk, Virginia. CID conducted a criminal investigation of Mr. Colaprete, Mom's Inc., and associated entities. According to Mr. Colaprete, IRS spent less than 48 hours investigating allegations that it had received from the company's bookkeeper before it obtained and executed search warrants on the two restaurants and the residences of Mr. Colaprete and an employee. Mr. Colaprete also complained about the conduct of agents during the execution of the warrants. He has filed a civil suit against employees of IRS and the state of Virginia. We attempted to interview IRS employees involved in the criminal investigation, the Department of Justice attorney handling the civil suit, Mr. Colaprete, and others involved with the restaurants. We were denied access to these individuals due to the ongoing litigation. Therefore, we discontinued our investigation of this matter. Mr. Colaprete's specific allegations and a summary of our discontinued investigation are included in enclosure VII.

[17] Richard Gardner owns and operates Gardner's Tax Service, Inc., a tax preparation service in Oklahoma. CID conducted a criminal investigation of Mr. Gardner that resulted in a 23-count indictment. Mr. Gardner alleged that the investigation and indictment were based on false information and that the IRS case agent had a personal vendetta against him. Allegedly, both the investigation and the execution of a search warrant were retaliatory against him because he had filed for bankruptcy protection, which prevented IRS from collecting the money he owed. Mr. Gardner filed a civil suit against the government for payment of his attorney's fees based on his allegation that IRS had a vendetta against him. The Department of Justice agreed to pay Mr. Gardner $75,000 but admitted no wrongdoing on the part of the government, including the IRS employees involved. Mr. Gardner's specific allegations and our investigative findings are included in enclosure VIII.

[18] Ray Cody Mayo practices tax law in Shreveport, Louisiana. He also represents IRS employees in employment-related suits against IRS. CID conducted a criminal investigation of Mr. Mayo. According to Mr. Mayo, it appears that IRS has targeted lawyers who represent taxpayers in an effort to intimidate and harass them. He believes that he was the target of such an attack. Mr. Mayo filed a civil suit against the IRS employee who, he believes, referred his case to CID as a result of a personal vendetta. This suit is currently pending. Mr. Mayo's specific allegations and our investigative findings are included in enclosure IX.

AGENCY COMMENTS

[19] In commenting on a draft of this letter, the Internal Revenue Service agreed with our findings. IRS also provided several technical comments and other suggestions that have been incorporated in this letter as appropriate.

SCOPE AND METHODOLOGY

[20] We conducted our investigation between May 1998 and March 1999. We reviewed the Committee's hearing files, the witnesses' prepared statements, and the hearing transcript We also obtained documentation from each hearing witness concerning the

specific cases they considered to be problematic. We obtained the official examination and/or investigative files for these cases as well as the investigative and audit files of IRSs Inspection Service. We reviewed IRS's policy and procedure manuals pertaining to audits and investigations, as well as our prior work and IRSs internal audit reviews.

[21] At the time of the hearing, the Inspection Service had either completed a review or had ongoing inquiries into several allegations raised at the hearing. It also initiated and has completed several other investigations as a result of testimony at the hearing. We did not attempt to duplicate the investigations conducted by the Inspection Service. However, as part of our investigation, we reviewed and analyzed the Inspection Service's investigative files and, in some cases, conducted additional interviews and records' analysis. The results corroborated and supplemented the Inspection Service's investigative findings. Some of the investigative files contained grand jury information, which was not provided to us pursuant to Rule 6(e) of the Federal Rules of Criminal Procedure. In addition, we contacted the Department of the Treasury's Office of Inspector General regarding any review or investigation it may have conducted on these cases. We did not assess the technical merits of the audit issues proposed in the specific case examples we investigated.

[22] We interviewed over 175 individuals involved with these specific cases. In one case, both the hearing witness and government employees declined our request to be interviewed due to a civil action. We discontinued our investigation of the case as a result of this limitation. A detailed explanation of the scope and methodology for each case is included in the respective enclosures.

* * * *

[23] As requested by your office, we will hold this letter's release for 30 days from the date of the letter. At that time, we will send copies of this letter to the Honorable Daniel P. Moynihan, Ranking Minority Member, Senate, Committee on Finance and to the Honorable Charles O. Rossotti, Commissioner of Internal Revenue. Because this letter contains tax return-related information, we will make no further distribution. If you have any questions or need additional information, please contact Deputy Director Donald G. Fulwider at (202) 512-6722.

Sincerely yours,

Robert H. Hast
Acting Assistant Comptroller
General
for Special Investigations

FOOTNOTES

[1] Tax Administration: Allegations of IRS Employee Misconduct (GAO/GGD-99-82).

[2] Tax Administration: Factors Affecting Results From Audits of Large Corporations (GAO/GGD-97-62, Apr. 17, 1997) and Tax Administration: Compliance Measures and Audits of Large Corporations Need Improvement (GAO/GGD-94-70, Sept. 1, 1994).

[3] The four witnesses on this panel were Ginger Jarvis, Michael Ayala, Maureen O'Dwyer, and Minh Thi Johnson.

[4] The additional IRS employee was * * *.

[5] In 1966, IRS established CEP to audit the nation's largest and most complex corporations, each with assets usually exceeding $250 million. A CEP audit team usually has an on-site team coordinator one or more revenue agents; and specialists, including economists and international examiners. A team coordinator directs the work of the agents and reports to a CEP case manager, who usually oversees several audits. CEP audit teams usually remain on-site at the corporation's headquarters for extended periods. The team generally examines two or three annual tax returns in a single audit cycle; each audit cycle takes an average of 2 to 3 years to complete.

[6] International examiners assigned to IEP audit domestic taxpayers and their foreign affiliates. The program is geared toward addressing significant deviations from arm's-length dealings or significant shifting of income to a foreign affiliate.

[7] GAO/GGD-97-62, Apr. 17, 1997, and GAO/GGD-94-70, Sept. 1, 1994.

[8] The four witnesses on this panel were William A Moncrief, Jr.; John Colaprete; Richard Gardner; and Ray Cody Mayo, Jr.

END OF FOOTNOTES

* * * * *

ENCLOSURE I ALLEGATIONS AND INVESTIGATIVE FINDINGS: GINGER M. JARVIS

INTRODUCTION

[24] Ginger M. Jarvis, a GS-13 revenue agent, assigned to the Coordinated Examination Program (CEP), was hired by IRS in January 1991. In April 1998, Ms. Jarvis testified before the Senate Finance Committee that millions -- even hundreds of millions -- of dollars in tax revenues owed to the U.S. Treasury by some of the largest taxpayers in this country are "literally forgiven, or zeroed out," at the sole discretion of individual managers. She added that this is an outrage that occurs because certain managers want to improve their statistics to gain status or personal awards or because they seek future careers with these large corporations. She described the following situations.

ALLEGATIONS AND FINDINGS

Allegation 1

[25] Ms. Jarvis stated that her analysis of the tax returns of a large consolidated group of companies strongly suggested that hundreds of millions of dollars had been laundered. She also stated that the IRS manager improperly removed her from the case for raising these concerns.

Investigative findings for Allegation 1

[26] Ms. Jarvis provided documents indicating that this allegation referred to * * *.

[27] Although the team coordinator did not remember all the issues, he told us that he recalled that he had not agreed with Ms. Jarvis. According to the team coordinator, he had presented Ms. Jarvis's opinions to the case manager who disagreed with Ms. Jarvis's application of the law. The case manager told us that he had had two other team members review the matter and that these persons also did not agree with Ms. Jarvis's assessment of the situation. When we interviewed these team members, they could not recall all the issues. However, they did recall that they had disagreed with Ms. Jarvis's application of the law. The case manager had also discussed the matter with a CEP team coordinator from another group who indicated that, based on the set of facts outlined by the case manager, the law relied upon by Ms. Jarvis would not apply. When we interviewed this individual, he could not recall the specifics of the conversation he had had with the case manager. He did recall that he had concluded that the law cited by Ms. Jarvis did not apply to the facts outlined, * * * which we reviewed.

[28] * * *

[29] The Inspection Service investigated the allegations raised by Ms. Jarvis, including the allegation that she had been improperly removed from this audit. [1] The Inspection Service found no evidence to substantiate the allegation that the case manager had improperly removed Ms. Jarvis. According to the investigator, when he offered to arrange a meeting between Ms. Jarvis and representatives from the Examination Division to discuss the merits of the issues she had raised, she declined the offer because "no one would believe her."

Allegation 2

[30] Ms. Jarvis stated that she discovered an abusive tax scheme in which nearly $400 million in taxable income had been potentially unreported for federal income tax purposes. She worked closely with IRS attorneys to develop the facts of the case over a 2- year period. She said that the district counsel had dropped the case and hundreds of millions of dollars of income were literally untaxed.

Investigative Findings for Allegation 2

[31] According to Ms. Jarvis, this case involved * * *

[32] * * * Ms. Jarvis's position is inconsistent with the IRS National Office's advice as well as the views of the Manhattan District Counsel and the Tax Court. [5]

[33] * * * officials in the Examination Division requested and received approval for an Information Gathering Project on * * *. The project eventually involved 35 districts and assessed * * * in taxes.

Allegation 3

[34] According to Ms. Jarvis, "cronyism is alive, well, and thriving" in the Manhattan District. She stated that she is aware of many cases that have been closed without making proper adjustments on the tax returns. In other cases, the recommendations made by the IRS employees for adjustments have not been followed, resulting in drastically reduced tax adjustments. Ms. Jarvis opined that these actions had occurred because of improper influence within the district. She explained that recently retired IRS managers represent clients before former colleagues who render favorable decisions for them. [6]

[35] According to Ms. Jarvis, in one case when a former IRS senior executive made unreasonable demands on behalf of his clients, "the. . . . [manager] stood . . . [her] ground and did not yield." Shortly after the meeting, the manager was assigned a temporary detail requiring extensive travel over a 4-month period. As a result, a substitute manager was brought in to manage the case. According to Ms. Jarvis, the substitute manager is widely known to be a close, personal friend of the former IRS senior executive who was representing the taxpayer. She added that shortly after the meeting with the former IRS executive and the substitute manager, the branch chief informed the assigned IRS attorney to close the case and to take no further action on it.

Investigative Findings for Allegation 3

[36] According to Ms. Jarvis, the former employee she was describing was * * * former * * *. The manager assigned * * * was Ms. Jarvis's * * * and the substitute Case Manager and the * * *, were * * * and * * *, respectively. Ms. Jarvis told us the case involved * * * and also included an international examiner from the International Enforcement Program (IEP).

[37] With regard to Ms. Jarvis's allegation, we found the following. First, * * * was not detailed because of the views she had expressed at the meeting with * * *, the former IRS senior executive who was representing * * * told us that she had been asked to assist the * * * and that * * * had no involvement or influence regarding the detail.

[38] Second, the Inspection Service investigated Ms. Jarvis's allegation that * * * and * * * had a close personal relationship [7] and could not substantiate the allegation. Instead the Inspection Service Report that addressed this allegation disclosed that on October 6, 1997, * * * had told the investigator that it was "common knowledge" that * * * and * * * were not close friends. In addition, Ms. Jarvis told the investigator that she asked * * * about his relationship with * * * and that he replied that he had met * * * on only four occasions. Moreover, * * * told us that his relationship with * * * was "strictly business."

[39] Third, we learned that * * *, not * * *, made the decision to close the case after she had returned from * * *.

[40] Fourth, officials in the Manhattan District Counsel Office told us that the * * * had not improperly influenced IRS attorneys who were assigned to the * * * audit, to take no further action on the audit. Specifically, they told us that the * * * had not instructed them to discontinue their work and that it would be highly unusual for a * * * to make such a suggestion. After reviewing the District Counsel Office's * * * case file, these officials

determined that * * * had called their office; however, there was no indication of the substance of that call. They told us that they did not recall any specific conversation with * * *.

[41] In addition to the evidence that we found regarding the three previously discussed allegations, we contacted a Manhattan District CEP Chief, Examination Branch, for his response to Ms. Jarvis's allegations. With regard to Ms. Jarvis's allegation that former IRS senior managers are representing clients before former colleagues with the expectation of receiving decisions favoring their clients, the CEP Chief told us that he is aware of the perception caused when former IRS officials represent clients before the IRS. He indicated that these individuals have an advantage in that they know the system and whom to call. He explained that this gains them access to individuals but nothing else. In addition, the former Acting Deputy Chief Inspector stated that the Inspection Service has received many allegations over the years concerning former IRS managers representing taxpayers before the IRS after they retire. He added that although there was a perception of wrongdoing in each of these cases, the Inspection Service has conducted many investigations where the allegations have not been substantiated.

[42] The CEP Chief also responded to Ms. Jarvis's allegation that managers had taken actions to zero-out tax liabilities of the largest taxpayers in the country to gain personal awards. Specifically, he told us that CEP has never emphasized no-changing cases and that there is no incentive in CEP to close an audit with no change. He also told us that the CEP no-change rate is historically lower than that of other audit programs.

Allegation 4

[43] Ms. Jarvis made numerous allegations about her former case manager. She said that she had witnessed what she believed was the case manager's operation of a private tax law practice at the audit site. She stated that the case manager had availed himself of the taxpayer's facilities and government staff to provide secretarial services for his personal gain. She added that the manager had previously conducted his private practice from the IRS office before relocating to the taxpayer's facilities in an upscale area in Manhattan.

Investigative Findings for Allegation 4

[44] According to Ms. Jarvis, the audit site was located at * * * and the manager involved was Case Manager * * *. The Inspection Service included these allegations in its investigation of Ms. Jarvis's allegations.

[45] The Inspection Service found evidence to support some of Ms. Jarvis's allegations. Although the Inspection Service did find that * * * had received prior approval for engaging in an outside legal practice and we verified this information, it did not find that the practice involved any federal, state, or city tax law litigation, as alleged by Ms. Jarvis. Instead the law practice involved matters such as real estate closings, adoptions, and divorce.

[46] However, the Inspection Service investigation did disclose possible evidence of * * * misuse of authority, time, and property. It found that on one or two occasions in 1988 or 1989, * * * had had a revenue agent leave the office early to drop off legal documents connected with the manager's private legal practice. It also found that on one occasion, another revenue agent had typed two or three short legal documents for * * *. Further, it found that * * * had written his IRS office telephone number on several personal business checks, indicating that he could be contacted at the IRS office.

[47] * * * said he never conducted personal business on government time and property. He admitted, however, that he might have asked an employee to drop off documents for him on the way home, as a favor, but never permitted any employee to leave early to do this. Although he does not recall doing so, he also stated that on occasion he might have asked someone on a lunch break to type a line or two or to copy a page or two for him regarding his outside practice.

[48] * * * told the Inspection Service that his work telephone number was on his personal business checks because the court (County Clerk's Office, New York and the Surrogate Service Court of New York) would not accept personal checks without a New York telephone number. He said he listed his work number because his law practice is located in New Jersey.

[49] On June 8, 1998, the Inspection Service forwarded the case to the U. S. Attorney's office in New Jersey for prosecutorial consideration. That office declined prosecution on July 30, 1998; and the Inspection Service concurred. As a result, the Inspection Service referred the matter to the Manhattan District for adjudication, resulting in the issuance of a reprimand.

SCOPE AND METHODOLOGY

[50] We interviewed revenue agent Ginger M. Jarvis on numerous occasions and obtained documentation regarding her allegations. We also reviewed her testimony before the Committee. We obtained and analyzed the Manhattan District's files concerning the specific cases identified by Ms. Jarvis. We interviewed the three supervisors who were involved with these cases, as well as knowledgeable senior Manhattan District managers. We also interviewed District Counsel Office attorneys, a technical advisor, and other revenue agents who were involved in these cases. In addition, we reviewed the Inspection Service's investigation report and supporting documentation concerning Ms. Jarvis's allegations about * * * and * * *, as well as specific allegations of improper conduct by her supervisor, * * *.

[51] Regarding the allegations concerning former IRS officials influencing audit outcomes, we interviewed the former IRS official named by Ms. Jarvis, the group manager involved, the district counsel, and an international examiner. We also obtained information from IRS's Office of Chief Counsel, Chief Ethics and General Government Branch. Further, we reviewed audit case files for the taxpayer and obtained a memorandum that documented the reasons for the actions taken.

FOOTNOTES TO ENCLOSURE II

[1] On Feb. 27, 1996, the Inspection Service initiated an investigation of these and other allegations received from Ms. Jarvis. The investigation was completed on Feb. 13, 1998.

[2] Ms. Jarvis received a Special Act Award on May 20, 1992, * * *. In addition, she was transferred to CEP and received a promotion from GS-11 to GS-12. * * *

[3] * * *

[4] * * *

[5] In * * * challenged IRS's determination that * * *. The tax court upheld the IRS determination. Hence, Ms. Jarvis's assertion at the oversight hearing that this case supported her position was incorrect.

[6] Government employees are subject to the postemployment restrictions in 18 U.S.C. section 207 when they leave the federal government. For example, under 18 U.S.C. section 207(a)(1), a lifetime prohibition prevents a former employee from seeking to influence any federal agency on behalf of a specific party in connection with a particular matter in which the former employee participated personally and substantially while employed by the government. In addition, under 18 U.S.C. section 207(a)(2)(B), a former employee cannot for a 2-year period seek to influence any federal agency on behalf of a person in connection with a particular matter that the former employee knows or should have known was actually pending under his responsibility within 1 year of his termination.

[7] In late 1997, Ms. Jarvis reported to the Inspection Service an alleged conflict of interest involving the audit of * * *. She stated that * * * had a close personal relationship with the former IRS employee, * * *. Ms. Jarvis said that * * * was employed with * * *, which was representing * * *.

[8] * * *

END OF FOOTNOTES TO ENCLOSURE I

ENCLOSURE II ALLEGATIONS AND INVESTIGATIVE FINDINGS: MICHAEL AYALA

INTRODUCTION

[52] Michael Ayala is a GS-13 analyst in the IRS Southeast Regional Office, Atlanta, Georgia. In April 1998, he testified before the Senate Finance Committee that he had worked for the IRS for over 30 years and that he had witnessed a broad range of misconduct by high-level managers in both tax administration and civil service practices. This misconduct included, among other things, mistreatment of taxpayers, covering up serious revenue losses and misconduct by executives, and improper use of enforcement statistics. He cited the following examples.

ALLEGATIONS AND FINDINGS

Allegation 1

[53] Mr. Ayala testified that certain members of IRS management in a particular district had forgiven over $30 million of an assessed $50-million tax liability for a large, influential business concern for no apparent reason. The remaining $20 million was allowed to be paid over a 5- to 6-year period. He added that IRS had also protected the company from levies and full tax liens being filed against it.

Investigative Findings for Allegation 1

[54] Mr. Ayala told us that he was referring to * * *

[55] * * * IRS's * * * District had been involved in an audit * * *.

[56] * * *

Allegation 2

[57] In another matter, Mr. Ayala told us that the Baltimore District had improperly closed out over 83,621 taxpayer cases -- that is, it closed the books on the cases without completing the process of collecting the taxes owed. This was done, according to Mr. Ayala, at a cost of millions of dollars to the public through the loss of uncollected taxes.

Investigative Findings for Allegation 2

[58] The Chief, Collections Division, Baltimore District, told us that Mr. Ayala's allegation involved the "Out of Business Project." According to a memorandum dated April 25, 1994, valuable revenue-officer resources were being used to collect taxes owed by out-of-business corporations; however, the collection potential of these taxpayers was minimal. As a result, the Out of Business Project was developed to streamline IRS's collection procedures. The project permitted the Mid-Atlantic Regional Office to close or expedite disposition of cases concerning out-of-business taxpayers prior to assigning them to a field revenue agent.

[59] In 1994, the IRS National Office granted authority to the Mid-Atlantic Region, which at that time included the Baltimore District, to survey (close) cases under the project. [2] Between mid- 1995 and September 1996, the Baltimore District closed approximately 83,000 cases. The Chief Compliance Officer, Southeast Region, [3] subsequently became concerned about the number of cases being closed by Baltimore and began questioning district officials about the matter. According to a memorandum from the Chief Compliance Officer dated September 25, 1996, the Baltimore District Chief of Collections provided six sample cases, which were representative of the cases being surveyed, to the Chief Compliance Officer. The Chief Compliance Officer determined that three of the six cases involved sole proprietors, even though only corporate taxpayers qualified for closing under the project.

[60] The regional office also asked for a review of all cases closed by the Baltimore District between March 1 and September 30, 1996, under the Out of Business Project;

and IRS's Internal Audit provided a listing of all the cases to district staff. An October 1996 review found problems with 82 percent of the cases.

[61] On January 30, 1997, the Baltimore District Director sent a memorandum to the Chief Compliance Officer outlining the district's plan to reactivate the cases closed improperly and address the concerns raised in the October review. According to a Collections Field Branch Chief, most of the closed cases were closed because they were uncollectible. For some of the cases, this meant just changing the closure codes from "surveyed" to "uncollectible." The entire reactivation effort was completed by March 1997.

[62] A Field Branch Chief in the Collection Division estimated that as a result of reactivating the survey cases, IRS collected less than $100,000. According to the Acting Chief of Collections, the cases that were closed were in the district's queue and likely would have remained there until the statute of limitations ran out had they not been pulled out as part of the survey project. Thus, most of the closed cases did not result in lost revenue to the IRS.

Allegation 3

[63] Mr. Ayala reported that the Baltimore District improperly closed 4,000 taxpayer cases in a project the IRS referred to as the "Low Dollar Study." He said this project created a situation that permitted inconsistent and unfair treatment of taxpayers. Further, a subsequent investigation of this matter by Internal Audit verified that the cases had been closed improperly and should be reassigned for corrective action.

Investigative Findings for Allegation 3

[64] The Baltimore District's Acting Chief of Collections told us the Low Dollar Study was another effort undertaken by the district to streamline IRS's collection procedures. Under this study, which began in November 1995 and ended on July 9, 1996, the Baltimore District was allowed to use minimal processing efforts to close the cases of individuals residing in certain areas in Delaware, Maryland, Virginia, and Washington, D.C., where revenue yield was low and compliance efforts were high. In addition to meeting the jurisdictional requirement, the cases selected were those of individuals having an adjusted gross income of less than $40,000 and an assessed tax due of less than $10,000. The Southeast Region estimated that the district processed 7,660 cases in the study from November 1995 to July 9, 1996.

[65] At the request of the Regional Chief Compliance Officer and the District Director, Internal Audit evaluated the Low Dollar Study, including inconsistent treatment of taxpayers, manual deviation requirements, and collectibility. Internal Audit's review found that from November 1995 to July 9, 1996, as a result of the study's efforts 217 installment agreements had been initiated; 541 liens, filed; 1,916 returns, filed; and $2,149,660, collected. In addition, Internal Audit found that the majority of cases processed by the district under the study met the minimal processing criteria. However, 823 cases (123 fell into more than one category) should not have been closed through streamlined processing because either they did not meet the district's selection criteria

or they contained attributes that suggested that they should not have been closed through that process.

[66] Internal Audit's review also noted that the district had not obtained formal approval to conduct the minimal processing test. Further, a concern existed that taxpayers had been treated differently, depending on the jurisdiction in which they lived. Finally, the review found that the test criteria had not been fully developed and supported.

[67] The audit recommended reopening those cases that had been improperly closed. On April 23, 1997, the District Director notified the Regional Chief Compliance Officer that with some exceptions, all 823 cases that had been processed improperly under the test would be reactivated. According to the District Director, the reactivation process began in February 1997 and was completed by August 1, 1997.

Allegation 4

[68] Mr. Ayala described one case in which misconduct involving a female employee was covered up. He said that the female employee had allowed a collection statute to expire and that IRS was therefore unable to collect $320,000. He said that her manager, who was involved in a relationship with her, had helped to cover this up.

Investigative Findings for Allegation 4

[69] Mr. Ayala, told us that this allegation refers to an incident that happened in July 1992 and that was brought to the Inspection Service on January 21, 1997. The female employee was a * * * in the Atlanta District Collection Division,and her duties included * * *

[70] * * *

[71] In 1994 the Collection Division conducted a review of problems encountered with the * * * courts in Georgia's three judicial districts. As a test, IRS sent several * * * in the same. Federal Express package to the * * * courts, including the one that should have received the * * * mailing * * * Although the court acknowledged receipt of several of the * * * on the package, it had no record of other * * * that had been sent in the same package.

[72] Neither a review by the * * * supervisors at the time nor a subsequent investigation by the Inspection Service established any wrongdoing by the * * * Furthermore, there was no evidence that the manager had attempted to cover up the incident or that the * * * had received special treatment or avoided disciplinary action.

[73] In his interview with the Inspection Service, the Chief, * * * Section, stated that based on his recollection of the issue concerning the * * * missing the bar date and review of the documentation, he believes the matter was handled in the customary manner. He also stated that numerous unresolved cases existed in which statutory bar dates had expired. Revenue officers working on those cases, according to the manager, were not treated any differently than the * * * in this case. Indeed, Mr. Ayala agreed that

only a pattern of missed bar dates, not a single instance, would result in disciplinary action.

[74] Regarding a personal relationship between the * * * and her manager, the relationship between the * * * and the then * * * began in * * * and ended in * * *. The relationship resulted in the birth of * * * in * * *. In * * *, the * * * informed IRS management about his affair with the * * * and the birth of * * *. He said that within hours he was removed from his supervisory position and placed in a "holding pattern". He said that he requested a transfer to the field as a revenue officer, which was granted, and he was reduced in grade from GS-13 to GS-12.

Allegation 5

[75] According to Mr. Ayala, the Southeast Region is tracking seizures from October 1995 through 1998, ranking the districts, and comparing the number of seizures made between districts and revenue officers. He said this was being done in blatant disregard of Policy Statement P-1-20 and the Taxpayer Bill of Rights. [4] According to Mr. Ayala, as long as enforcement comparisons continue to be applied and used as performance measures for revenue officers as well as districts, abuses in this area will naturally follow.

Investigative Findings for Allegation 5

[76] We identified the employee of the Southeast Region who prepared a report entitled "Seizures Southeast Region [Fiscal-Year] 97." The report contained charts showing the number of seizures made per district and graphs illustrating the number of seizures made per revenue officer in each district. According to the employee and another senior compliance analyst, this report was prepared without the supervisor's knowledge or request.

[77] After reading the report, the employee's supervisor contacted the employee and expressed concern over his choice of words, noting the information could be viewed as evaluative, which was prohibited. The employee stated that when he prepared the report, he was aware of the prohibition on using enforcement statistics for evaluative purposes and that he had not intended the report for that purpose. Following Mr. Ayala's Senate testimony, four IRS managers reviewed the report and determined that it was improper. Another senior compliance analyst agreed that someone could conclude, as Mr. Ayala testified, that the region was tracking seizure figures at district offices, that the region tracked seizures by officer, and that the region provided opinions on the value of seizures (i.e., "improved," "second place," "slipped," and "disappointing"). According to IRS officials, no action was taken against the employee who had prepared the report.

Allegation 6

[78] According to Mr. Ayala, he reported to the EEO office the presence of a striptease performance in the Atlanta Regional Office during office hours after hearing about the incident. He added that he had not attended the birthday celebration where the incident occurred. Mr. Ayala stated that he considered his conversation with the EEO officer to be a complaint against his supervisors for allowing the incident to occur. He said that

the EEO officer told him she would look into the matter. He also said that the EEO Officer reported his contact with her to his supervisors and attempted to dissuade him from pursing the matter. Mr. Ayala stated that when he persisted, the Regional Commissioner subjected the entire regional staff to sensitivity training. However, no action was taken against either the person responsible for having the stripper in the office or the "high-level executive manager" who approved it.

Investigative Findings for Allegation 6

[79] According to a memorandum written by the manager who approved the party, a birthday celebration had taken place in the Atlanta Office on October 21, 1992, which included a "stripper" from a business called Eastern Onion. The manager stated she was told that the stripper had not undressed.

[80] * * * Southeast region, told us she recalled the incident mentioned by Mr. Ayala in his testimony. She said that she learned from an EEO specialist about the incident soon after it had happened. At about the same time, the Regional Commissioner came into her office and asked her about it. According to * * * she told the Regional Commissioner that she had just been notified and immediately had called the EEO counselor in the division where the incident had occurred to learn any additional details. At approximately the same time, according to her, Mr. Ayala reported the incident to her. She said she did not inform him she was already aware of the matter and that her office was conducting a review of the incident. According to * * *, Mr. Ayala came back a second time to report that a videotape was made of the incident; and although she had already reviewed the tape by this time, she did not share this information with Mr. Ayala. She said neither Mr. Ayala nor anyone else filed an EEO complaint at that time over this matter.

[81] * * * said the Southeast Region held a mandatory meeting for all staff to discuss the striptease incident, stress the inappropriateness of such matters, and ask that all staff engage in appropriate behavior at work in the future.

[82] * * * also said that while Mr. Ayala claimed that no one was reprimanded for the incident the manager was admonished for her actions. A memorandum reflecting the admonishment was given to her, and a copy was placed in her file.

SCOPE AND METHODOLOGY

[83] We interviewed analyst Michael Ayala, obtained documentation from him, and reviewed his testimony before the Committee. With regard to Mr. Ayala's concerns about surveying a large number of cases, we met with Baltimore District officials involved in the various actions and obtained documentation that addressed the issues he raised. As to the conduct allegations in the Atlanta District Office, we met with Atlanta District officials and obtained information that addressed Mr. Ayala's concerns. Further, we obtained the Inspection Service's internal audit reports concerning the cases about which Mr. Ayala testified. We also reviewed the Inspection Service's investigation report and supporting documentation pertaining to the allegation of a

cover-up in exchange for sexual favors. In addition, we interviewed the employees involved with this allegation.

FOOTNOTES TO ENCLOSURE II

[1] * * *

[2] In Apr. and May 1994, the Mid-Atlantic Region issued guidelines for survey authority. In Feb. 1996, Headquarters Operations staff wrote a manual supplement to the 1994 survey authority. The Chief, Collections Division, stated that this supplement provides "somewhat" stricter guidelines for surveying cases.

[3] After IRS's reorganization, the Baltimore District was transferred to the Southeast Region on Oct. 1, 1995.

[4] Since 1973, IRS Policy Statement P-1-20 has prohibited using records of tax enforcement results to evaluate enforcement officers or to impose or suggest production goals or quotas. In 1988, the Omnibus Taxpayer Bill of Rights, Pub. L No. 100-647, section 6231, 102 Stat. 3734 (1988), also prohibited the use of records of tax enforcement results to evaluate collections employees. The IRS Restructuring and Reform Act of 1998, Pub. L. No. 105-206, section 1204,112 Stat. 722 (1998), repealed section 6231 of the Omnibus Taxpayer Bill of Rights by expanding the evaluation prohibition to cover all IRS employees. In addition, Inspection Service's Internal Audit issued three reports regarding the use of enforcement statistics: Examination Division's Use of Performance Measures and Statistics, 084303, July 7, 1998; Use of Enforcement Statistics in the Collection Field Function, 081904, Jan. 12, 1998; Review of the Use of Statistics and the Protection of Taxpayer Rights in the Arkansas-Oklahoma District Collection Field Function, 380402, Dec. 5, 1997.

END OF FOOTNOTES TO ENCLOSURE II

ENCLOSURE III ALLEGATIONS AND INVESTIGATIVE FINDINGS: MAUREEN O'DWYER

INTRODUCTION

[84] Maureen O'Dwyer is a GS-13 international examiner in the Manhattan District. She has worked for IRS for approximately 12 years. In April 1998, Ms. O'Dwyer testified before the Senate Finance Committee that the system of taxation is dependent on the taxpayer's, belief that the tax laws will apply to everyone and that they will be administered impartially. She alleged that there is uneven enforcement of the Internal Revenue Code and regulations by some IRS managers. She cited the following examples.

ALLEGATIONS AND FINDINGS

Allegation 1

[85] Ms. O'Dwyer stated that she had examined a taxpayer's return and orally proposed adjustments that involved issues regarding transfer pricing, reorganizations, mergers, and consolidations. The dollar amount of the proposed adjustments was in excess of $42 million. Her manager ordered her to no-change the case without adjustments.

Investigative Findings for Allegation 1

[86] According to Ms. O'Dwyer, this case involved the audit of * * *

[87] * * *

[88] In March 1996, her * * *, conducted a workload review [1] of Ms. O'Dwyer's cases and noted that * * * had been open for approximately 5 years and was far from being concluded. * * * concluded that even though Ms. O'Dwyer had spent over 1,400 hours on the case, additional work was necessary to close the case.

[89] * * *

[90] * * * action was in keeping with a March 21, 1996, memorandum from the District Program Manager to all International Examination Managers, including * * * The memorandum contained instructions to close all overage, unagreed cases by April 1996 and all overage, agreed cases by May 1996. (Overage cases are those that have been in process more than 12 months and 5 months for revenue agents and tax auditors, respectively.) It also stated that there would be no exceptions, excuses, or deviations. The list of cases to be closed included * * *.

[91] According to * * * all IEP cases, whether closed with or without adjustments require an International Examiner's report. This report describes issues considered and explains why an adjustment was or was not made. Ms. O'Dwyer included the following remarks in the International Examiners Report for * * *.

[92] * * *

[93] The Inspection Service conducted an investigation of Ms. O'Dwyer's allegations but did not find evidence that supported her allegations. The Assistant Chief, Examination Division, told the Inspection Service and us that after reviewing the file, he believed the decision to close * * * was a sound business decision and in accordance with the Internal Revenue Manual. * * * said * * * had estimated that it would take more than a year to complete the case.

Allegation 2

[94] Ms. O'Dwyer provided information about complaints that a revenue officer had concerning actions he was forced to take against two taxpayers. Ms. O'Dwyer provided the testimony because the revenue officer was afraid of retaliation if he testified.

[95] Ms. O'Dwyer stated that the revenue officer had written off as uncollectible two taxpayer accounts. His manager had threatened disciplinary action against him if he refused to take action to collect the taxes. On Christmas Eve, the manager "brutally" forced the revenue officer to levy the salary of one taxpayer earning only a subsistence

wage. The second taxpayer, dying of cancer, was living on welfare. The manager ordered the revenue officer to have the taxpayer provide a written statement and supporting documentation that would verify his financial condition and illness. Ms. O'Dwyer concluded that in incidents such as this, employees are intimidated and coerced into submitting to the manager's misused authority with resultant inequitable actions that harm taxpayers.

Investigative Findings for Allegation 2

[96] We interviewed both the revenue officer and his manager and reviewed available files regarding the cases discussed in Ms. O'Dwyer's testimony. The revenue officer stated that on December 24, 1997, in reviewing one of his case files, his manager learned that * * * The revenue officer stated that (1) * * * without consulting the revenue officer was improper and (2) taking action on Christmas Eve, although legal, sent an abusive message.

[97] The manager described the revenue officer as * * * The manager recalled the case in which he had directed the revenue officer to * * *. On December 24, 1997, the manager was reviewing the revenue officer's case files and noted that * * *. He also noted that * * *

[98] According to the revenue officer in the second case, * * * in addition, the revenue officer stated that the manager had inappropriately * * * without first talking to him about the proposed call. * * * Although the manager told us that he had no recollection of this case, he stated that the revenue officer's work performance * * *.

Allegation 3

[99] Ms. O'Dwyer testified that a Manhattan District administrator was arrested for a violation of a civil statute. She stated that the employee was never discharged and is now in a "superior" position.

Investigative Findings for Allegation 3

[100] Ms O'Dwyer told us that she was referring to * * *, who at that time was * * *.

[101] * * * told us that she was not arrested for any reason. She said that at one point she had many * * *

[102] Her supervisor then asked her for an explanation and for the details of the incident she said she was subsequently removed from a * * * position and given a 3-day suspension for "causing embarrassment to the IRS." She was reassigned to an * * * position in the the * * * Office and later was assigned to the position of * * *. She said this is an administrative position and does not know how anyone could mistake it for a "superior" position.

SCOPE AND METHODOLOGY

[103] We interviewed Maureen O'Dwyer, reviewed her testimony, and obtained additional documentation concerning her allegation about the audit of * * * Further, we

contacted the individuals that Ms. O'Dwyer identified as having first hand knowlegde of the issues she raised in her testimony. One of these individuals refused to meet with us, while another denied that the incident had occurred. We interviewed a third individual, * * * and included his allegations in this report.

[104] Regarding * * *, we obtained and analyzed the audit files for this company. We interviewed the two * * * supervisors, a technical advisor, and Manhattan District senior managers with knowledge about this case. Further, we reviewed the Inspection Service's investigation files and reports directly relevant to Ms. O'Dwyer's concerns about this case; and we interviewed the investigator.

[105] During the hearing, Ms. O'Dwyer testified on behalf of a Manhattan District revenue officer who was afraid to testify about his manager's abuse of taxpayers. In her testimony, she provided two specific examples of these abuses. We interviewed this revenue officer and his manager and obtained a relevant file concerning one of these cases.

[106] Regarding Ms. O'Dwyer's allegation that a Manhattan District manager was arrested and later promoted, we interviewed the individual named in the allegation and obtained relevant documentation from the Manhattan District.

FOOTNOTE TO ENCLOSURE III

[1] Workload reviews provide a basis for evaluating a revenue agent's or examiner's performance and can provide constructive feedback for continuing or terminating examinations.

END OF FOOTNOTES TO ENCLOSURE III

ENCLOSURE IV ALLEGATIONS AND INVESTIGATIVE FINDINGS: MINH THI JOHNSON

INTRODUCTION

[107] Minh Thi Johnson is a GS-12 revenue agent in the Los Angeles District. IRS hired her in January 1991. In April 1998, Ms. Johnson testified before the Senate Finance Committee about alleged abuses by IRS employees. She cited the following examples.

ALLEGATIONS AND FINDINGS

Allegation 1

[108] MS. Johnson stated that the district director had reduced the negotiated settlement concerning taxes assessed in an examination in which she was involved. In regard to this matter, Ms. Johnson testified that when she was in the IRS Los Angeles District Office a $35-million settlement was negotiated with a taxpayer on a $70- million assessment However, her group manager refused to accept the $35-million check. Not long after, the district director and the district counsel took over settlement negotiations, and a $22-million settlement was accepted. Ms. Johnson believes that the district

director lowered the settlement amount to ingratiate himself with the taxpayer's representatives in an effort to secure a postretirement position. She added that one of the taxpayer's representatives was a former IRS district director.

Investigative Findings for Allegation 1

[109] When we interviewed Ms. Johnson, she could not provide the name of the taxpayer. However, she did provide the name of her former group manager, who had retired. We contacted the former manager, obtained information about the case, and determined that the audit had been completed during 1996. The former manager provided several names of individuals involved with this audit. She stated that Ms. Johnson had had no involvement either directly or indirectly in the case.

[110] We contacted two revenue agents who were responsible for the audit and the former district counsel. They provided specific details of the audit, * * *. They also stated that Ms. Johnson had not been assigned to the audit. One of the revenue agents and the former group manager described the case as extremely complex and sophisticated, involving a taxpayer that had a * * *

[111] According to the revenue agent's, * * *. The former group manager and the former district counsel stated that the district director did not attempt to influence the * * *

[112] Ms, Johnson's former manager confirmed that one of the taxpayer's representatives involved with the case was a former Los Angeles * * *. However, he was not involved in * * *

Allegation 2

[113] Ms. Johnson stated that her supervisor might have initiated an IRS audit of Ms. Johnson's husband, Eric Johnson. She added that soon after her husband had asked Ms. Johnson's manager to stop IRS employees from harassing Ms. Johnson, her husband received a notice that he was being audited.

Investigative Findings for Allegation 2

[114] Mr. Johnson stated that he had a discussion with his wife's supervisor in August 1996. He received the notice of an audit of his 1994 return either the same or the following month. According to Mr. Johnson, he was not concerned about being audited but rather about the timing of the audit.

[115] Our investigation revealed that * * * Moreover, Ms. Johnson's supervisor denied to us having knowledge of * * *.

SCOPE AND METHODOLOGY

[116] We interviewed Minh Thi Johnson and reviewed her testimony. Although Ms. Johnson was unable to provide any information that would identify the specific taxpayer or the examination involved with the settlement that she described in her testimony, we located and interviewed former and current IRS personnel who were able to provide specific information. With regard to the tax audit of Ms. Johnson's husband, we

interviewed Ms. Johnson and her husband; * * * and interviewed an official of the Chief of Examination Division, IRS Los Angeles District Office. We also interviewed the supervisor alleged to have initiated the audit of Mr. Johnson.

ENCLOSURE V ALLEGATIONS AND INVESTIGATIVE FINDINGS: * * *

INTRODUCTION

[117] * * * is a GS-13 international examiner with the Manhattan District and has worked for IRS since May 1994. We contacted him during the investigation of allegations raised by Maureen O'Dwyer (see enclosure III). * * * told us that he had knowledge of two former IRS managers who now work for major accounting firm who have used their former associations with current managers to influence audits. He cited the following examples.

ALLEGATIONS AND FINDINGS

Allegation 1

[118] * * * stated that he believes a * * * audit was improperly influenced by former IRS manager * * *

Investigative Findings for Allegation 1

[119] According to information provided by * * * and from a review of the * * * audit workpaper files, * * *.

[120] * * * was formerly the * * * for the International Examination Program in the Manhattan District. He retired from IRS on * * * and is employed by the accounting firm, * * * representing * * * before IRS. When we interviewed * * * he was unable to provide any specific information as to how * * * improperly influenced the audit.

[121] However, * * *, * * * former manager in the International Examinations Group stated that * * * alleged that * * * had exerted pressure to have * * * removed from the audit. According to * * * complained to * * *. According to * * * called him after * * * had learned of the complaint and threatened to report him to the Inspection Service and the Director of Practice. According to * * *, * * * told * * * that he felt * * * was attempting to limit the scope of the audit. * * * advised * * * in writing that he should not tell representatives that he would report them to the Inspection Service or the Director of Practice when they had done nothing wrong. * * * also instructed * * * to follow instructions and to treat taxpayers and representatives professionally.

[122] * * * who became the manager of the International Examination Group in * * * after * * * departure, also received complaints about * * * from several taxpayers, including * * * immediately after taking over the group. Representative of * * * other than * * * complained about * * * conduct during the audit, which included unannounced visits and inappropriate comments to a * * * employee. * * * told us that he conducted a workload review of * * * after receiving these complaints and later removed * * * from the * * * audit.

[123] * * * stated that at the time he conducted the workload review, he instructed * * * to summarize a * * * issue that * * * alleged had involved * * * did not comply with this instruction. * * * * also told us that a domestic internal revenue agent, to whom the * * * were reassigned, reviewed the audit workpaper files. He found information that explained how the * * *.

[124] We contacted the Inspection Service and were informed that * * * had filed a complaint in 1998 and that the case is still under investigation. While this investigation is not complete, the investigator told us that the preliminary results do not support * * * allegations. The inspector assigned to this investigation told us that * * * has not been able to describe how * * * received preferential treatment.

[125] We also contacted IRS's Office of Chief Counsel, Chief Ethics and General Government Law Branch, to determine whether this office had provided any advice to * * * concerning postemployment conflicts of interest. This office provided documentation showing that after * * * was assigned the audit of * * * he wrote the Office of Chief Counsel to determine whether there where any postemployment restrictions against his representing * * * In August 1996, the Office of Chief Counsel responded that based on the information * * * and the Manhattan District Office had provided, he could represent * * * He reasoned that the 2-year restriction in 18 U.S.C. section 207(a)(1) was inapplicable because * * * had not had official responsibility for IRS's examination of * * * while employed by IRS. We attempted to speak to * * * about this case. While he provided information about his past employment with IRS, on advice of * * * counsel, he would not discuss problems he had had with * * * regarding the * * * audit.

[126] We also examined documents * * * We introduce below some excerpts from the International Examiner's Report, prepared by * * * to illustrate these points.

[127] * * *

[128] We also learned that the disposition of this issue involved differences in interpretation of the rules. In this regard, * * * told us that * * * felt that * * *. According to * * * who is currently the district's * * *

[129] * * *

Allegation 2

[130] Mr. Arcilla stated that he believes that former IRS manager * * * improperly influenced the * * * audit. He added that * * * has avoided paying taxes because of * * * influence and the assistance and cooperation of group managers and other individuals in the International Examination Branch. He alleged that the group managers have dropped numerous multimillion-dollar clear-cut, statutory, and taxable audit issues (including penalties).

Investigative Findings for Allegation 2

[131] According to information provided by * * * and from a review of the * * * audit * * *.

[132] * * * was formerly employed with IRS as the * * * He retired from the IRS in * * * and is employed by the accounting firm, * * * representing * * * before IRS. When we interviewed * * * he said that * * * had exerted influence to alter the outcome of his examination but did not provide any specific information. He also stated that * * * had exerted pressure to have him removed from the audit.

[133] According to * * * to * * * the Internal Revenue Code and related tax cases require that * * *

[134] In response to questions concerning possible influence by former IRS personnel working for the taxpayer, * * * stated that no representations or inducements had been offered to him to influence his decision in the * * * tax matter.

[135] According to * * * was present at the time Messrs. * * * agreed to close the * * * audit. Part of this agreement involved * * * Subsequently, * * * sent a letter to * * * requesting additional information for * * * called * * *, complained about the letter, and requested that * * * not be involved in the * * * audit. It was thereafter assigned to another international examiner.

[136] We also examined documents that reflected the * * *. We introduce below some excerpts from the International Examiner's Report, prepared by * * * that reflect these points.

[137] * * *

[138] * * * told us that he contacted the Inspection Service and filed a complaint concerning * * * actions. We contacted the Inspection Service, which confirmed that * * * had filed a complaint in 1998. The Service told us that the cases is still under investigation. While this investigation is not complete, the investigator told us that the preliminary results do not support * * * allegations. The inspector assigned to this investigation told us that * * * has not been able to describe how * * * received preferential treatment.

[139] We contacted IRS's Office of Chief Counsel, Chief Ethics and General Government Law Branch, to determine whether this office had provided any advice to * * * concerning postemployment conflicts of interest. The office provided us documentation showing that * * * had written the Office of Chief Counsel to determine whether he had any postemployment restrictions representing clients before IRS. In July 1995, the Office of Chief Counsel responded that since * * * had no direct involvement in any particular case, and, thus, did not participate "personally" and "substantially" in a matter involving a specific party, the lifetime postemployment restriction in 18 U.S.C. section 207(a)(1) did not preclude him from representing clients before IRS.

SCOPE AND METHODOLOGY

[140] Ms. O'Dwyer testified before the Senate Finance Committee hearings, in part, about * * * concerns. We interviewed * * * on several occasions, reviewed Manhattan District files, and interviewed district employees who were involved in the two cases he cited as examples of his concerns. These interviews included the three supervisors that

* * * had during the audit of these taxpayers, the economist, involved, and the branch chief. We also contacted the two former IRS officials named in the allegation. One former official, on advice of counsel, would not discuss problems he had had with * * * We contacted IRS's Office of Chief Counsel, Chief Ethics and General Government Branch, concerning the postemployment advice it had provided these individuals about representing clients before IRS. Further, we interviewed the Inspection Service's investigators about the ongoing investigation of certain allegations made by * * *.

FOOTNOTES TO ENCLOSURE V

[1] Under 26 U.S.C. section 482, IRS has authority to distribute, apportion, or allocate gross income, deductions, credits, or allowances between two or more businesses, organizations, or trades if it determines that such action is necessary to prevent evasion of taxes or to clearly reflect the income of the entities. In the case of any transfer (or license) of intangible property, the income with respect to such transfer or license shall be commensurate with the income attributable to the intangible.

* * *

END OF FOOTNOTES TO ENCLOSURE V

ENCLOSURE VI ALLEGATION AND INVESTIGATIVE FINDINGS: WILLIAM A. MONCRIEF, JR.

INTRODUCTION

[141] William A. Moncrief, Jr., is the president of a family- owned company, Montex Drilling Company, which is involved in oil and gas development. Its headquarters is located in the Moncrief Building, Fort Worth, Texas. On September 1, 1994, IRS's Criminal Investigation Division (CID) executed a search warrant on the Montex headquarters. William Moncrief testified in April 1998 before the Senate Finance Committee and raised concerns about the way IRS had investigated his company and related entities.

ALLEGATION AND FINDINGS

Allegation

[142] William Moncrief questioned why IRS did not issue a summons or subpoena. He stated that IRS agents had stormed the offices like an army on an enemy beachfront. He added that they had rummaged over every inch of the building, barking orders and threatening to kick down doors. According to William Moncreif, one agent said he would blow the hinges off the safe if it was not opened. These agents left with over 1 million documents and an entire computer system. Further, IRS "terrorized" his employees, knocking on doors at their homes.

[143] William Moncrief added that the case was initiated as a result of information provided to IRS by a former Montex in-house accountant who had stolen information

from the company. According to William Moncrief, this employee had been fired for incompetence. William Moncrief also claimed that the $23 million he agreed to pay in settlement of the case had been arbitrarily determined and was the result of extortion.

Investigative Findings

[144] With regard to the allegation that the search warrant was issued improperly and that the IRS agents acted inappropriately in executing the warrant, we found that a U.S. Magistrate had issued a search warrant on August 29, 1994, for the offices of Montex. According to the Assistant U.S. Attorney, the U.S. Attorney's Office and IRS had taken extra steps and precautions to ensure that all policies, procedures, and laws were followed throughout this investigation. For example, * * * In addition, the Assistant U.S. Attorney requested that IRS videotape the execution of the warrant, use a "low-key" entrance, and wear business suits. He also reviewed the raid plan, which he does not normally do.

[145] * * *

[146] According to the IRS and Montex employees that we interviewed, the agents wore business attire (business suits and not raid jackets). Although the agents carried their service weapons, the witnesses told us that at no time did any agents draw their weapons during the search.

[147] * * *

[148] The company's vice president, Charlie Moncrief (the son of William Moncrief), stated that he arrived while the search was being conducted, as did attorneys representing the Moncriefs. He told us that the IRS agents had conducted themselves "relatively well," calling one particular agent a "gentleman," although he characterized some as "wise asses." Other Montex employees we interviewed stated that the agents were not physically or verbally abusive but were "firm," "stern," or not "cordial." They told us that some agent's guns were visible when they removed their suit jackets while conducting the search. A Moncrief attorney remained until the search was completed at approximately 5:00 p.m. This attorney stated that when he arrived, only 4 or 5 Montex employees were present and no one complained of mistreatment b the agents.

[149] Richard Moncrief (another son of William Moncrief), an employee of Montex, reported that as a result of the search, slate tile flooring in the entry of the building was damaged, which may have been the result of moving heavy file cabinets. In addition, a section of drywall adjacent to Charlie Moncrief's office was removed; Moncrief's attorney speculated that agents may have removed; Moncrief's attorney speculated that agents may have removed it, possibly expecting to find hidden documents. According to Charlie Moncrief, most of the business records were returned by November 1994. Before then, IRS allowed the Moncriefs to retrieve from IRS the records needed to continue their business.

[150] The only complaints the Assistant U.S. Attorney recalls from Mr. Moncrief's attorneys regarded the use of a search warrant instead of a subpoena and the number

of IRS personnel used in the execution of the warrant. Regarding the use of a search warrant rather than a subpoena, the U.S. Attorney stated * * *

[151] * * * In addition, according to the Assistant U.S. Attorney, a large number of agents were used to facilitate seizure of a large volume of records and to allow the Moncrief Building to be searched in a timely fashion.

[152] We interviewed several Montex employees who were contacted by IRS agents at their homes after the warrant had been executed. They advised us that they were not threatened or harassed by the agents; however, two employees stated that they refused to answer the door when an agent appeared at their homes. Agents did not attempt to interview employees at their homes after they had retained counsel.

[153] As to William Moncrief's allegation regarding Montex's former in-house accountant, our review of the case files and interviews of IRS employees show the following. * * * Further, the Assistant U.S. Attorney involved in this case stated that it was legal to accept these documents under these circumstances.

[154] * * *

[155] We also investigated William Moncrief's allegation that the settlement amount was arbitrarily determined and resulted from extortion. We learned that during the summer of 1995, while the investigation was ongoing, the Assistant U.S. Attorney received a call from the Moncriefs' attorney. The attorney wanted to determine whither a civil settlement could be reached. Upon receipt of a written request from the Moncriefs' attorney to settle this case, * * *

[156] * * * The U.S. Attorney stated that neither the Moncrief family nor its attorneys ever contacted him to complain about the fairness or validity of the agreement.

Inspection Service Investigations

[157] IRS's Inspection Service conducted four separate investigations involving allegations of IRS abuse and misconduct concerning the Moncrief criminal investigation. In September 1994, the Inspection Service received information through the Secretary of the Treasury from an anonymous source alleging that the IRS agents had acted inappropriately when serving the search warrant. The Inspection Service closed this case in October 1994, stating that no evidence had been found to support the complaint.

[158] A second investigation was initiated * * *.

[159] The third and fourth investigations began in March 1997, when the US. Attorney's Office forwarded to the Inspection Service two letters it had received from Mr. Moncrief's attorney in January 1997. One letter outlined 16 allegations of misconduct against IRS personnel. This investigation found no criminal or administrative misconduct by IRS personnel as to these allegations. The second letter alleged that * * *.

SCOPE AND METHODOLOGY

[160] We attempted to interview William Moncrief; however, he was not available because of his poor health. We interviewed two of his sons -- Charlie Moncrief, the company's vice president, and Robert Moncrief, a company employee. We obtained and reviewed documents from the company. Further, we interviewed other employees of Montex and two attorneys for the Moncriefs. We also interviewed the U.S. Attorney for the Northern District of Texas, the Assistant U.S. Attorney who was assigned to the Moncrief investigation, IRS criminal investigators, a revenue agent, and an estate and gift tax attorney. Further, we interviewed an investigator regarding the Inspection Service's four investigations of William Moncrief's allegations, and we reviewed the reports and supporting documentation. We reviewed the Moncrief criminal investigation file, which included the affidavit for the search warrant. We also reviewed the videotape of the execution of the search warrant. We analyzed * * * and the * * *.

FOOTNOTES TO ENCLOSURE VI

[1] * * * According to the Apr. 1999 review of IRS's CIR by the Honorable William H. Webster, both IRS and CID management interpret this directive as requiring CID to employ the least intrusive means needed in its investigations. * * *

/*/ A nolo contendere is a plea in a criminal case that subjects the defendant to a conviction without.

END OF FOOTNOTES TO ENCLOSURE VI

ENCLOSURE VII ALLEGATIONS AND INVESTIGATIVE FINDINGS: JOHN COLAPRETE

INTRODUCTION

[161] John Colaprete and Theodore Bonk own Mom's, Inc., which operated two restaurants in Virginia Beach and Norfolk, Virginia. Richard Miller was the manager of the Virginia Beach restaurant. In April 1994, IRS's CID, with the assistance of agents from the Department of Alcoholic Beverage Control (ABC) of Virginia and police officers from the Norfolk and Virginia Beach police departments, executed search warrants on both restaurants and the residences of Messrs. Colaprete and Miller.

ALLEGATION AND FINDINGS

Allegation

[162] Mr. Colaprete stated that IRS had executed the search warrant based solely on the word of the company's bookkeeper, a multiple felon, and after spending less than 48 hours investigating the bookkeeper's allegations. According to Mr. Colaprete, the IRS accepted the bookkeeper's allegations as true despite a lack of substantiation or proof. Mr. Colaprete added that the bookkeper had been kept in protective custody and allowed to leave Virginia even though there was an outstanding warrant for her arrest.

[163] Mr. Colaprete further stated that armed agents accompanied by drug dogs had stormed his restaurant during breakfast, interrogated his employees, and ordered his patrons out of the restaurant. IRS impounded records, cash registers, and computers. The front door of his home was torn off its hinges, his dogs were impounded, his safe was seized, and his house was left in shambles. According to Mr. Colaprete, a watch was missing from the safe when the safe was returned to him. Mr. Colaprete added that Mr. Miller had been pulled from the shower at gunpoint and forcibly restrained and that his son was knocked to the floor. He said that at the time of the search warrant's execution, Mr. Miller's daughter was having a slumber party and the girls were forced to get dressed under the watchful eyes of a male agent, with his gun drawn.

Investigative Findings

[164] Messrs. Colaprete, Bonk, and Miller, among others, together with Mom's, Inc., have filed a civil lawsuit against agents of the federal government (IRS), the state of Virginia (ABC), and the cities of Virginia Beach and Norfolk for damages. The lawsuit asserts that the IRS and others engaged in an unlawful search and seizure, assault and battery, intentional infliction of emotional distress, and negligence.

[165] We attempted to interview a number of persons concerning Mr. Colaprete's allegations. However, with a few exceptions, we were not able to do so because of the civil litigation. Because of this limitation, we discontinued our investigation of the matter.

SCOPE AND METHODOLOGY

[166] We reviewed the hearing transcript of John Colaprete's testimony and documents he provided to us. We reviewed the affidavit for the search warrants. We interviewed several officials with the Virginia Department of Alcoholic Beverage Control, Norfolk City Police Department, Virginia Beach Police Department, and Virginia Attorney General's office. We made preliminary contact with employees of IRS and the Department of Justice who were involved in this investigation. We attempted to interview these officials and were informed that because of the civil litigation, the individuals were not available. Similarly, although we had preliminary contact with Mr. Colaprete, we were informed that he and his associates would not be available for interview until after the civil litigation had been completed.

ENCLOSURE VIII ALLEGATIONS AND INVESTIGATIVE FINDINGS: RICHARD GARDNER

INTRODUCTION

[167] Richard Gardner owns and operates Gardner's Tax Service, Inc., a tax preparation service in Oklahoma. In April 1998, before the Senate Finance Committee, he testified to abuses by IRS during its investigation of him. He stated that in March 1995, agents of IRS's CID executed a search warrant at Gardner's Tax Service. Subsequently, a federal grand jury investigated allegations against Mr. Gardner. In March 1997, the grand jury returned a 23-count indictment charging MR. Gardner with aiding and assisting the preparation of false tax returns, concealment Of assets in bankruptcy, and bankruptcy fraud. In May 1997, the U.S. Attorney FIled a superceding

indictment changing some of the bankruptcy- related counts. Between May 1997 and January 1998, the court dismissed all 23 counts.

ALLEGATION AND FINDINGS

Allegation

[168] Mr. Gardner stated that IRS's investigation had been initiated as retaliation for his filing for bankruptcy protection and that the execution of a search warrant was a continuation of this retaliation. He also stated that IRS's investigation and the grand jury's subsequent indictment were based upon false information and that the IRS case agent had told two employees of Gardner's Tax Service that he had a personal vendetta against Mr. Gardner. According to Mr. Gardner, IRS seized all of his clients' tax returns, his computer, and other records in an attempt to put him out of business by denying him information. Further, IRS agents harassed and intimidated witnesses.

[169] In March 1998, Mr. Gardner raised these allegations in a civil suit [1] claiming that the conduct of the IRS's criminal investigation was vexatious, frivolous, and in bad faith. He argued that he was entitled to reimbursement of his attorney's fees.

Investigative Findings

[170] Based a review of the CID investigative reports and interviews of IRS employees, we found * * *.

[171] In regard to Mr. Gardner's allegation concerning the IRS investigation in 1995 and subsequent indictment, we found the following * * *.

[172] Based on that warrant, IRS seized client files, documents, and computers. Although Mr. Gardner alleged that the seizure was an effort to put him out of business by denying him access to his business information, Mr. Gardner and his employees were provided access to the documents that had been seized during the search.

[173] * * * Although Mr. Gardner was indicted on 23 counts charging him with aiding and assisting the preparation of false tax returns, concealment of assets in bankruptcy, and bankruptcy fraud, the U.S. District Court subsequently dismissed all 23 counts.

[174] The assistant U.S. attorney who was assigned the gardner investigation provided the following reasons for the dismissal of the 23-count indictment against Mr. Gardner:

[175] * * *

[176] Mr. Gardner's attorney contacted the Chief of CID Arkansas-Oklahoma District alleging improprieties during the investigation of Mr. Gardner. The Chief of CID referred the matter to the Inspection Service, which subsequently conducted an investigation. The Inspection Service concluded in July 1998 that there was no evidence of improprieties by IRS agents. However, two of the five witnesses identified in the indictment told us they had felt intimidated and harassed in having to deal with IRS during the investigation. The other three witnesses stated that they did not believe they were intimidated or harassed by the process or by any IRS employee. IRS's Inspection

Service also interviewed witnesses involved in the Gardner investigation who stated that IRS agents did not intimidate or harass them. Two employees of Gardner's Tax Service stated that the case agent told them that he had had a personal vendetta against Mr. Gardner for 15 years. The case agent denied having made that statement.

[177] In January 1999, Mr. Gardner's civil suit against the government for payment of his attorney's fees was settled. Mr. Gardner claimed that he had incurred $108,332 in attorney`s fees and expenses. The Department of Justice agreed to pay Mr. Gardner $75,000 but admitted to no wrongdoing on the part of the government. According to the U.S. Attorney

SCOPE AND METHODOLOGY

[178] We interviewed Richard Gardner and his attorney and reviewed his testimony and hearing transcripts. We also interviewed an employee of Gardner's Tax Service, the IRS case agent for the Gardner investigation, his supervisor, and the Chief of IRS's CID, for the Arkansas-Oklahoma District. Although we were not able to obtain grand jury information, we did review IRS's investigation files and reports and the affidavit for a search warrant. We interviewed the U.S. Attorney for the Northern District of Oklahoma and the Assistant U.S. Attorney responsible for the investigation of the Gardner case. We discussed the case with certain Department of Justice officials in the Executive Office of the U.S. Attorney and reviewed pertinent court pleadings and correspondence in the case. We interviewed clients of Mr. Gardner who alleged that IRS had intimidated them. Further, we reviewed the Inspection Service's report and supporting documentation that addressed the allegations raised by Mr. Gardner.

FOOTNOTES TO ENCLOSURE VIII

[1] On Mar. 3, 1998, Mr. Gardner filed an Application and Authority for Assessment of Attorney Fees against IRS, citing Pub L. No. 105-119, section 617, 111 Stat. 2519 (1998), otherwise referred to as the Hyde Amendment. The Hyde Amendment allows individuals who were under criminal investigation to sue the government for payment of legal fees and other costs in cases where the government's actions were vexatious, frivolous, or in bad faith.

[2] * * * According to the Apr. 1999 review of IRS's CID by the Honorable William H. Webster, both IRS and CID management interpret this directive as requiring CID to employ the least intrusive means needed in its investigations.

END OF FOOTNOTES TO ENCLOSURE VIII

ENCLOSURE IX ALLEGATIONS AND INVESTIGATIVE FINDINGS: RAY CODY MAYO, JR.

INTRODUCTION

[179] Ray Cody Mayo, Jr., practices tax law in Shreveport, Louisiana. He also represents IRS employees in employment-related suits against IRS. Mr. Mayo's wife,

Elizabeth S. Mayo, is a practicing physician. In April 1998 before the Senate Finance Committee, Mr. Mayo stated that he was the subject of a criminal investigation by IRS's Cid for failing to file federal income tax returns for the years 1990, 1991, and 1992. Mr. Mayo testified about IRS abuses during his criminal investigation. This investigation was discontinued in March 1994.

ALLEGATION AND FINDINGS

Allegation

[180] Mr. Mayo stated that it appears that IRS had directly targeted lawyers who represent taxpayers in an effort to intimidate and harass them. He believed he had been a target of such an attack. In 1992, and 1993, Mr. Mayo was representing a small business corporation in audit proceedings before IRS. During a meeting with an IRS Examination Division group manager and an internal revenue agent, he alleged that he was threatened by the manager with an audit of his personal finances. Subsequently, CID began investigating Mr. Mayo. He believes that the manager who referred him for criminal investigation acted out of a personal vendetta. Mr. Mayo also alleged that the manager illegally disclosed his tax information when he showed a former IRS employee a copy of Mr. Mayo's tax account before he referred his case to CID.

[181] Mr. Mayo added that after "months of torture," IRS dropped the criminal investigation and continued an audit that ended with a "no change" letter. He stated that IRS's own records showed that he had made a substantial overpayment and that IRS knew it from the very beginning. However, after the criminal investigation was complete, IRS continued a campaign of harassment over a period of years.

Investigative Findings

[182] Mr. Mayo told us that in April or May 1993, while representing a client before IRS, he met with Examination Division Group Manager * * * and Internal Revenue Agent * * *. He recalled that during this meeting, * * * had become enraged and stated, "Maybe we just ought to audit you." * * * denied making the threat, and * * * told us that he does not recall the threat having taken place. Further, IRS's Inspection Service conducted an investigation of this allegation and did not find evidence to corroborate Mr. Mayo's complaint. * * * told the Inspection Service that he had never heard * * * threaten to have anybody audited, including Mr. Mayo.

[183] Based on research performed by the Inspection Service, [1] we learned that * * *.

[184] * * * As for Mr. Mayo's assertion regarding the motive of the individual who referred the case to CID, * * *.

[185] * * *

[186] To the extent that Mr. Mayo alleged that IRS had engaged in "months of torture" against him, we found the following.

[187] As for Mr. Mayo's allegations that IRS continued a campaign of harassment after closing the criminal investigation, knowing that he had made an overpayment, we were told that * * *.

[188] In order to investigate Mr. Mayo's disclosure of tax information by an IRS employee, we interviewed several individuals. Specifically, Mr. Mayo told us that * * * and * * * former IRS revenue officers with the Collection Division, informed that before they retired, * * * had shown them a copy of Mr. Mayo's transcript before the case was referred to CID. However * * *.

SCOPE AND METHODOLOGY

[189] We interviewed Ray Cody Mayo and reviewed his testimony before the Committee. We also interviewed current and former IRS revenue agents and revenue officers, including the manager who * * *.

[190] The Inspection Service investigated the allegations that Mr. Mayo had raised at the April 1998 hearing before the Senate Finance Committee. We reviewed the Inspection Service's report and supporting documentation. This documentation included analysis of * * *.

FOOTNOTE TO ENCLOSURE IX

[1] The inspection service opened an investigation on Apr. 24, 1998, based on Mr. Mayo's Apr. 1998 testimony before the Senate Finance Committee. It completed the investigation on Oct 30, 1998, and issued a report on Nov. 6, 1998. The Inspection Service reviewed * * *.

END OF FOOTNOTE TO ENCLOSURE IX

Tax Analysts Information

Code Section: Section 7213 -- Unauthorized Disclosure
Geographic Identifier: United States
Subject Area: Practice and procedure
Legislative tax issues
Index Terms: tax administration
IRS, employee offenses
IRS, employee offenses, reports to Congress
compliance, examinations
Institutional Author: General Accounting Office; Office of Special Investigations
Tax Analysts Document Number: Doc 2000-11630 (52 original pages)
Tax Analysts Electronic Citation: 2000 TNT 80-13
Cross Reference:

Senator KERRY. Could we also, because some Senators, I know, wanted to pose a few questions who couldn't be here, just leave the record open for a week or something like that?

Chair SNOWE. Yes, we will, to about March 8th.

Senator KERRY. For written questions. Obviously, there's a difference of opinion here, and we're not going to sort it out today. I want to try to see if we can just give a little more meat to it.

Finance Committee staff have been in touch with our staff. Those Finance Committee staff have documented the notion that they had a hard time, that they didn't get the names of witnesses until the day of the hearing or that there were documents that were even withheld. Someone even said that apparently some documents were kept in the trunk of your car. Is that true?

Mr. THORSON. We had a person in our office who was sending things to the IRS before the hearings. We felt that was going on. We knew that was going on. We knew it was going on after we left the office. There were times when we would take things out with us just simply to make sure that people in the office couldn't have access to them.

Senator KERRY. Did that keeping things from access take place on a partisan basis, or was it——

Mr. THORSON. It had nothing to do with politics. In fact, the person I'm talking about was on our—the Republican staff.

Senator KERRY. Did it result in some people therefore not being able to have access or something, or did it create an air of—I'm just trying to——

Mr. THORSON. I don't know. I mean, first of all, like I said—and believe me, I'm not ducking your question; we're talking about 8 and 9 years ago, and I don't really remember—I do know that as far as the staff having access, we weren't operating in a vacuum, obviously. This was a huge investigation for Senator Roth as well. He watched—he was very proactive in this and knew everything that we were doing.

He had counsel, Frank Polk, who I'm very proud of the fact is here in the room today, representing Senator Roth very well. And——

Senator KERRY. Well, I understand that. I'm just trying to understand—because later on, and I'm confident that there are always two sides to these things. The GAO didn't come to you, I understand, to try to ascertain some of these things because they went to the actual facts of the cases.

Here's what they themselves wrote. Let me just read you what they said. This is their conclusion.

> "Based on our investigation, we did not find any evidence to support the allegation that IRS managers' decisions to 'no change' or 'zero out' proposed tax assessments were improper. However, our investigation established that the allegations themselves had been based on an incomplete awareness of the total circumstances surrounding the matters."

They also found—I'm skipping down here a little bit—

> "Generally, we found no corroborating evidence that the criminal investigations described at the hearing were retaliatory against a specific taxpayer. Further, we found no evidence that IRS employees had acted improperly in obtaining and executing the search warrants."

Finally, I think they also—well, let me just—I mean, those are sort of factual findings as a result of going—they also found that the 8 specific cases were not substantiated by the facts.

Mr. THORSON. Well, I would——

Senator KERRY. That's a pretty dramatic sort of contradictory statement.

Mr. THORSON. Yes. I disagree with their—for instance, let's talk about the affidavit for search warrant. In one of the cases, in the Colaprete case, which was the Jewish Mother Restaurant, they say, "Well, there were lawsuits here, so we couldn't really interview and therefore we don't want to assume anything." But there was no real evidence.

Wait a second. There was an application—there was a bookkeeper who was accused by Colaprete days before of embezzlement. She went to the FBI, to the ATF, and both of them rejected her, and so she went to the IRS. Within 48 hours, they executed a search warrant.

The facts that they very easily could have found, if they had bothered—and I'm not trying to be critical here of GAO, but I am having to defend myself here on this—she had a record. She had a prior record of embezzlement. That would have been very easy to determine. We knew that. In the case of an affidavit for search warrant, they should have—they're supposed to have two corroborating witnesses. They did not.

One of your own—or Senator Snowe's own staff pointed out to me that a Federal judge ruled that the IRS lied on that affidavit for search warrant. Of course, the easiest one was, "Was this true? Did she embezzle from this restaurant when at the same time she's trying to get the IRS in?" Yes. She was convicted of stealing—I think it was either $30,000 or $60,000. She was convicted for that, of that same restaurant. When they say there were no facts to corroborate this, I have a really hard time with that.

In another case—and I won't drag this on, but I appreciate very much the way you've been approaching this, and it's very valid—all charges were dismissed against a tax preparer. There were 23 counts. All counts were dismissed, and the Justice Department ended up paying him $75,000 in settlement. Now, that doesn't in itself explain everything, but it's sure a pretty good indication that maybe this wasn't right.

I've got one of those for almost every single example they've listed here. It's simply by reading their own statement. What I think you are reading from, and forgive me if I'm making an assumption here, but in the summary up front where they give you the findings, it's terribly negative. I think it's pretty much what you just read. If you go into the report, which I've now read many times, and you read the lines, the actual statements—and I've got it by page number—they verify this stuff. This happened.

What we don't agree on is the motivation. Nobody questioned that it was within the discretion of the manager to zero out those tax bills. That's what they're saying. It was done properly. No question it was. Why did he do it? That was the problem. That gets to the whole issue of oversight.

These are auditors and interviewers. We're supposed to exercise a different level of judgment in working for you all. I took that re-

sponsibility very seriously. I interviewed these people. I talked to them. I talked to other people in their offices.

Senator KERRY. Let me ask you this. Let me sort of shortcut this a little bit because of the time. I'm not trying to cut you off at all.

Mr. THORSON. That's all right.

Senator KERRY. I appreciate your answer enormously. Assuming you're confirmed for this job, is there a lesson you feel you take out of those hearings, out of that process, that you would apply in this job as Inspector General? I mean, is there something, sort of a message about different views and the contentiousness of that, that leaves you saying, okay——

Mr. THORSON. Oh, I'll never forget the contentiousness.

Senator KERRY. Therefore, does that affect how you might approach this job as IG?

Mr. THORSON. Yes, sir. To some degree, it does. Yet in another, it doesn't. What we do up here, and what I did as a congressional investigator, is really different than what you would do as an IG and working with the professionals who do the audits and do the criminal investigations. I do think there's a bit of a difference.

The thing I think you're getting at and I agree with is you've got to be really, really careful. One of the things, though, that I'm hoping that Senator Roth and his immediate staff and his counsel would agree with is, we were really careful because we represented him. He, above anyone else I've ever worked for, exemplified integrity and character.

I just—there are some similarities, yes, and there are some lessons learned, certainly. I never dreamed that we would run into some of the kind of problems we ran into after doing those hearings. The American people loved them, and they thought the world of the Senate, and certainly Senator Roth gained from them.

For me personally, yes, sir, I think I have to—when doing these kinds of things, you have to be very, very careful in how you approach them. I also trusted these people that I had vetted, and I listened to them, and I stand behind them today. If I have to lay the GAO report next to the testimony, I'm going to stand behind my witnesses. They were telling the truth. They were scared, and they were under oath.

Yes, sir, there are some lessons there that I will obviously carry with me the rest of my life. That was a huge event in my life.

Senator KERRY. Well, Mr. Thorson, I appreciate your comment. There is a letter here that I just ask to be part of the record from Donald Fulwider, who was the author. He responded to the specific questions of Senators. I would ask that that be made part of the record by the Chair.

Chair SNOWE. Without objection, so ordered.

Senator KERRY. Thank you.

[Letter from Mr. Fulwider follows:]

March 1, 2006

Senator John F. Kerry
Senator Carl Levin
U.S. Senate
Washington, D.C.

Dear Senators:

This letter is in response to your letter dated February 27, 2006, regarding the Government Accountability Office's (GAO) study of the 1997 and 1998 Senate Finance Committee hearings on the Internal Revenue Service. On May 24, 1999, GAO's Office of Special Investigations (OSI) issued a restricted report to the Senate Committee on Finance (GAO/OSI-99-9R). At the time the study was conducted, I was the Deputy Director for Investigations with OSI; lead the study; conducted interviews; reviewed documentation; and was the principle author of the report.

The following is my response to the questions contained in your letter:

1) At the time of GAO's investigation into the 1997-1998 hearings, how many years of experience did you have in the federal government and as an investigator with GAO?

   In 1999, I had approximately 27 years of investigative experience of which 12 years was with GAO.

2) At what point was your office contacted by the Finance Committee to conduct an investigation into the claims made in either the 1997 or the 1998 hearings? At what point did your office begin the investigation that resulted in the May 24, 1999, report to Finance Committee Chairman Roth?

   GAO's Office of Special Investigations (OSI) was contacted by Committee staff shortly after the 1997 hearing; however, the Committee did not request an investigation. Chairman William V. Roth, Jr. contacted GAO the same day as the 1998 hearing and requested an investigation into the allegations raised at the hearing. The issues raised in the request letter were divided between GAO's program area (General Government Division) and OSI. OSI initiated its investigation in May 1998. GAO's General Government Division issued a separate public report (GAO/GGD-99-82).

3) According to the information collected during your investigation, do you believe that Eric Thorson was the primary Finance Committee staff person responsible for conducting the investigations that resulted in the Finance Committee hearings on IRS taxpayer and employee abuses in 1997 and 1998?

   Yes, at both the meetings I attended concerning the 1997 and 1998 hearings Mr. Thorson was described as the lead investigator.

4) To what extent did the testimony provided at the hearings differ from the information that GAO obtained during the course of its investigation?

   Based on our investigation, we did not find any evidence to support the allegations raised by IRS employees that IRS managers' decisions to "no-change" or "zero-out" proposed tax assessments were improper. The witnesses were correct in some of the facts supporting their allegations in some of the cases. However, our investigation established that the allegations themselves had been based on an incomplete awareness of the total circumstances surrounding the matters. Further, we found no corroborating evidence that the criminal investigations described at the hearing were retaliatory against the specific taxpayer.

5) If the facts uncovered by GAO differed materially from those presented at the hearings, to what extent were these differences attributable to the nature and thoroughness of the investigation conducted by Mr, Thorson? During the GAO investigation, did you find evidence that Mr. Thorson had conducted similar due diligence, such as interviews with supportive witnesses, in order to substantiate claims made by those who testifies before the Committee?

   As part of our investigation we reviewed the Committee's hearing file, the witnesses' prepared statements, and the hearing transcript. As I recall, the Committee's hearing file contained some data and documentation provided by individual witnesses, which provided little assistance to the investigation. As a result, we began our investigation based on the hearing record. I do not recall the hearing file containing any information that indicated an effort on the part of Committee staff to corroborate or substantiate the allegations.

6) Do the findings of the GAO investigation raise questions about the thoroughness of the due diligence conducted in the Finance Committee's investigation?

   At the time we requested access to the Committee's hearing file we thought we would obtain information that would have corroborated the allegations raised at the hearing. However, this information was not in the hearing file.

7) To what extent did the Finance Committee investigative team, led by Mr. Thorson, provide documented evidence of the due diligence performed in conducting this investigation? Please include a description of what GAO found in terms of interview notes, the number and quality of the interviews conducted, and the evidence of efforts undertaken by Mr. Thorson to substantiate specific allegations of IRS misconduct.

   As I previously stated, I do not recall the hearing file containing any information that indicated an effort on the part of Committee staff to corroborate or substantiate the allegations. Currently, I am unable to quantify the type and extent of the hearing file. I do recall that the information contained in the hearing file did not contain information that furthered the investigation. As a result, we began our investigation based on the hearing record.

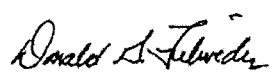
8) Given the discrepancy in factual evidence provided by the GAO and the Senate Finance Committee, in your professional opinion, do you believe that a thorough, independent investigation was conducted to substantiate the claims made by witnesses prior to their testimony before the Committee?

   As I recall, the Committee's hearing file did not contain information that indicated an effort to corroborate or substantiate the allegations made by the witnesses that testified before the Committee.

9) In your professional opinion, does the GAO investigation raise questions about the qualifications of Mr. Thorson to serve as the Inspector General of the Small Business Administration?

   The GAO investigation concluded some of the information provided by witnesses at the hearing was inaccurate, incomplete, and/or out of context. A more thorough investigation, by Committee staff, prior to the testimony would have prevented this from happening.

Sincerely,



Donald G. Fulwider

U. S. Small Business Administration
Office of Inspector General

SBA-OIG
2003-2007
Strategic Plan

Fall 2002

OFFICE OF INSPECTOR GENERAL

Message from the Inspector General

Fall 2002

I am pleased to present our 2003-2007 Strategic Plan, which describes our primary areas of focus for the next 5 years. The U.S. Small Business Administration (SBA) operates in a dynamic environment. Our ability to maximize our relevance and value to the SBA is closely linked to how well we adapt our work within that changing environment and our ability to effect change. Based on our analysis of the key issues facing SBA and a review of our own internal operations, we have established the following five strategic goals:

Strategic Goal 1 – Prevent fraud and unnecessary losses in SBA programs

Strategic Goal 2 -- Improve the security over and the accuracy of SBA accounting and management information, including performance data

Strategic Goal 3 -- Assist SBA in improving its small business development programs

Strategic Goal 4 -- Assist SBA management in identifying and resolving persistent and emerging management issues

Strategic Goal 5 -- Strengthen our ability to identify and have maximum impact on the most significant SBA issues

Our strategic plan also sets a new focus for how we carry out our work – emphasizing prevention and deterrence, early identification of risks and management challenges, and a more integrated approach within and across our audit, investigations and inspections functions.

Over the next 5 years we are committed to using this strategic plan as a framework to develop our annual plan and budget, and to report on progress. At the same time, we are pragmatic and recognize that planning is a dynamic and iterative process. Therefore we will continue to scan our environment and modify our direction as needed.

The SBA OIG recognizes that it occupies a position of trust within the SBA and with the U.S. Congress. We have embraced this responsibility. I am confident in our approach and welcome the opportunity to discuss any aspect of this plan.

Phyllis K. Fong

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SBA-OIG Strategic Plan 2003-2007

SECTION 1 INTRODUCTION

This 2003-2007 Strategic Plan (Strategic Plan) presents the Small Business Administration (SBA) Office of Inspector General (OIG) priorities for the covered timeframe. It serves an important purpose in succinctly describing our strategic direction to our stakeholders, including the SBA Administrator and the U.S. Congress. From that perspective, it presents our results-based business case, explaining our return-on-investment.

It also strengthens OIG by establishing a shared set of expectations regarding the goals we expect to achieve and the strategies that we will use to do so. We will adjust the plan as circumstances necessitate, use it to develop our annual plan and budget submission, report on progress in our semiannual reports, and hold our managers and staff accountable for achieving the goals and outcomes.

Given the importance of this Strategic Plan to our future operations, the constraints that were encountered during the planning process need to be highlighted. In a "best case" scenario, we would identify the major risks confronting the SBA and focus the majority of our resources on mitigating them. The reality, however, is that a considerable percentage of our resources are devoted to other necessary activities, such as auditing the SBA financial statements, responding to complaints about potential wrong-doing, and responding to requests from the SBA, Congress, and the public. As a result, the level of resources that we can devote to discretionary priority areas is significantly constrained.

The remainder of this document presents those planning elements that we thought essential for providing a sense of long-range direction to stakeholders and employees. It answers the key question, "How will the work we do and our approach to work change over the next 5 years?" This section includes our mission, a succinct statement regarding our vision, and the values that characterize our culture. In order to provide a context for our strategic goals, we present a brief summary of major issues confronting the SBA in ***Section 2 – Situational Assessment.*** This information, and an assessment of our internal challenges, served as a basis for the five strategic goals presented in ***Section 3 – OIG Strategic Goals, Performance Measures, and Strategies.***

The plan concludes with ***Section 4 - Relationship of this Strategic Plan to Our Annual Performance Plan, Budget, and SemiAnnual Reports to the Congress***. We present additional detail regarding how we will use this strategic plan in the coming years to meet our annual planning, budgeting, and day-to-day management responsibilities. While readers are likely to be very interested in <u>what</u> we plan to do over the strategic timeframe, understanding <u>how</u> we expect to do those things is equally important.

OUR MISSION

Under the authority and in fulfillment of the Inspector General Act of 1978, as amended (IG Act), the Inspector General is committed to supporting SBA in its statutory mission to maintain and strengthen the Nation's economy by aiding, counseling, assisting, and protecting the interests of small businesses, and by helping families and businesses recover from disasters.

Statutory Responsibilities

OIG is an independent and objective oversight office created within the SBA by the IG Act. The Act specifies that the Inspector General will:

- Promote economy, efficiency, and effectiveness in the management of SBA programs and supporting operations;
- Conduct and supervise audits, investigations, and reviews relating to the Agency's programs and support operations;
- Detect and prevent fraud and abuse;
- Review existing and proposed legislation and regulations and make appropriate recommendations;
- Maintain effective working relationships with other Federal, State, and local governmental agencies, and non-governmental entities regarding the mandated duties of the Inspector General;
- Inform the SBA Administrator and Congress of serious problems and recommend corrective actions and implementation measures;
- Comply with the audit standards of the Comptroller General; avoid duplication of General Accounting Office (GAO) activities; and
- Report violations of law to the U.S. Attorney General.

OIG also has other significant statutory responsibilities. They include responsibilities under the:

- Small Business Act
- Small Business Investment Act of 1958
- Federal Managers' Financial Integrity Act of 1982
- Chief Financial Officers Act of 1990
- Right to Financial Privacy Act
- Freedom of Information Act, and
- Privacy Act

Five divisions carry out these responsibilities: Auditing, Inspection and Evaluation, Investigations, Counsel, and Management and Policy.

OUR VISION FOR FY 2003 THROUGH FY 2007

SBA will have efficient, effective, results-oriented, integrity-based programs that maximize use of safe and secure information technology in its operations, and will have

minimal losses from fraud, abuse, erroneous payments and inadequate processes. OIG will be an effective catalyst to help SBA achieve this goal.

SECTION 2 SITUATIONAL ASSESSMENT

The SBA is engaged in substantial strategic and tactical change. It is dramatically altering how it administers its lending program, is modernizing its information technology systems, and is placing increasing emphasis on the business development aspects of its mission. These changes are complex and challenging. They affect many Agency programs and activities. Such dramatic changes also imply substantial risk in many areas such as making prudent decisions, effectively and efficiently developing, implementing, and operating the programs, ensuring that adequate management and internal controls are present, and ensuring that the changes better position the SBA to provide maximum return-on-investment to the American taxpayer.

This context poses a major challenge for OIG. Our current and future activities must balance our routine responsibilities and involvement in these SBA tactical and strategic changes to ensure that potential risk issues are adequately addressed. Consequently, we selected the three most dominant issues and present the following discussion to inform readers about their associated magnitude and complexity. This information provides the context for our strategic goals, which are presented in Section 3.

About the SBA

The SBA mission is to maintain and strengthen the nation's economy by aiding, counseling, assisting, and protecting the interests of small business and by helping businesses and families recover from natural disasters.

SBA administers small business programs, including 8(a)[1] Federal contracting set-asides and 7(a)[2] loans to help economically disadvantaged firms start, grow, and stay in business. SBA's disaster loan program offers financial assistance to businesses and families trying to rebuild in the aftermath of a disaster.

[1] Sec. 8(a), Small Business Act, 15 USC 637 (a): SBA's Section 8(a)program assists in the development of small companies that are owned and operated by socially and economically disadvantaged individuals. A Section 8(a) company is eligible for Federal contracting set-asides and other business development support to gain access to the economic mainstream.

[2] Sec. 7(a), Small Business Act, 15 USC 636 (a): the 7(a) loan program is for business start-ups and to meet the varied short- and long-term needs of existing small businesses. Under 7(a), SBA guarantees loans to small businesses that cannot obtain financing on reasonable terms through other channels.

Issues Confronting the Small Business Administration

Risks Associated With Increasing SBA Reliance on Private Sector Lenders

SBA has substantially changed its business model relative to how it delivers and services its loan products. Under a strategy to privatize more of its operations, the Agency is moving farther away from the direct delivery of products and services and instead is using its partnerships and business resource partners more extensively. Over the past

several years, SBA has been in the process of selling off assets in its loan portfolio and relying on private lenders to perform an increasing percentage of the loan underwriting, servicing, and liquidation functions that were previously performed by SBA staff. Consequently, SBA's need to monitor the activities of lenders who help deliver its programs has increased significantly in recent years. Annual loan approvals have almost doubled since 1992, and the loan portfolio for all its programs now exceeds $40 billion. During that same time, SBA has decreased its staff by 20 percent and shifted to lenders the responsibility for key loan origination, servicing, and liquidation functions. Lenders now originate about 75 percent of new loans, with little or no involvement by SBA in the eligibility and credit approval processes.

This shift has substantially changed the way that SBA does business and was the impetus for SBA's decision to undertake a major reengineering of its lending and oversight functions. Implementing these new business processes, which will be supported by modernized state-of-the-art information systems, is integral to SBA's success and will be a key strategic effort over the next several years.

These changes entail substantial risk for fraud and abuse. Lack of direct involvement in lending and servicing functions impair SBA's ability to prevent and detect fraud in its loan programs. Consequently, the new business structure must include adequate compensating controls. Over the next 5 years, our work will devote resources to assessing and mitigating this risk (see goals 1 and 4).

Risks Associated with SBA Efforts to Improve Information Technology (IT) Infrastructure, Management, and Security

In conjunction with the reengineering effort, SBA is embarking on a comprehensive Agency-wide modernization initiative to replace a range of outmoded legacy systems. This multi-phased, multi-million dollar effort is designed to improve decision-making through the collection of accurate and timely information and increase productivity and cost-effectiveness of service delivery to SBA customers. The scope of the project includes the development of new systems for:

- Capital access and credit programs
- Integrated financial management systems (i.e. accounting, human resource and procurement) and disaster assistance
- Government contracting and entrepreneurial development programs

This initiative is key to improving SBA's lender oversight functions, as well as its ability to produce accurate and useful financial management data. In addition to new application systems, the project also involves implementing a new IT infrastructure including a new telecommunications network and upgraded office computing systems. The new infrastructure is needed to support data interchange, communications, information sharing, and e-government.

To ensure effective management of its IT assets, SBA is in the process of implementing an IT investment review process that complies with the requirements of the Clinger-

Cohen Act and the provisions of OMB circular A-130. The process will provide a framework for evaluating IT projects and managing the associated risks.

SBA has also taken steps to improve security over its information systems, developing an enhanced security program, expanding IT security staff, developing updated security policies, reviewing sensitive systems, and developing critical infrastructure protection and security plans. Full implementation of all aspects of the security program will require continued attention and the devotion of resources to this critical issue over the next several years.

The implementation, management and security of these high-cost, high-risk systems will be a key area of focus for OIG (see goals 2 and 4). We will work with the SBA to identify and reduce risks associated with large systems development and to improve IT management and security.

Risks Associated with Increasing SBA Emphasis on Small Business Development

The SBA has two primary areas of emphasis – it provides small business financing services and conducts programs focused on developing small businesses. Two ways SBA supports this latter responsibility is by:

- Providing access to Federal procurement markets through its small business contracting programs and
- Providing entrepreneurial development assistance, through a range of delivery channels such as Small Business Development Centers (SBDCs), the Service Corps of Retired Executives (SCORE), Women's Business Centers, Business Information Centers (BICs) and One-Stop Capital Shops.

As SBA reviews and adjusts its approach in these areas, it will encounter substantial challenge and risk. Ensuring that these programs are focused on results (per the GPRA) and are able to measure progress in achieving them will be a challenge. The SBA will also face challenges in ensuring that small businesses have access to Federal procurement opportunities. Federal agencies have streamlined their acquisition practices, such as multiple award contracts, Federal supply schedules, and credit card purchases, making it more challenging for small businesses to compete.

In the area of entrepreneurial development assistance, SBA will work to integrate its entrepreneurial services programs. These programs evolved independently over time, taking various approaches to meet a range of small business needs. SBA will also work to better integrate its entrepreneurial services with its financing programs. During the planning period, OIG will analyze the efficiency and effectiveness of these programs to identify opportunities to reduce costs and better support the Agency's mission.

Implications for OIG

Given the preceding discussion, we formulated five strategic goals, described in detail in the next section. Taken in totality, these goals represent how we plan to align our resources and manage our activities. The goals are summarized in the following table.

SUMMARY OF OIG SBA STRATEGIC GOALS

The following information summarizes OIG SBA strategic goals. The table summarizes current initiatives that will continue during the planning period and new initiatives that reflect our strategic direction. The change in balance between current and future activities has significant OIG implications, discussed at a high level in the fourth column.

Strategic Goal	Ongoing Initiatives	New Focus or Initiatives	Implications for OIG
Goal 1-Prevent fraud and unnecessary losses in SBA programs	• Currently scheduled and planned audits, including early default audits • Criminal, civil and administrative investigations • Limited outreach to lenders • Review borrowers that self-declare having a prior criminal record • Affirmative Civil Enforcement (ACE)	• Expand educational outreach to lenders & SBA officials regarding fraud prevention and detection • Analyze internal Agency data to identify trends and patterns of fraud • Review criminal history on all non-citizens with FBI • Work with SBA program officials to develop fraud indicators in agency lender reviews • Review Non-citizen loans project • Review 8(a) eligibility • Lender relations/ethics training	We will need to emphasize education, prevention, and deterrence, adjust our culture in terms of incentives and rewards, increase the use of multi-disciplinary approaches, and improve how we analyze information to identify risks, trends, and patterns.
Goal 2-Improve the security over and accuracy of SBA accounting and management information, including performance data	• Financial statement audits • Follow-up reviews to assess implementation of additions to new financial system • GISRA audits • Prioritize participation in new systems development and include appropriate staff representation on SBA project teams.	• Select a statistical sample of the most critical data for selected key programs and determine the quality of data used to report on performance results. • Increase involvement in development of new automated systems including e-Gov initiatives • Assist Agency in review of performance monitoring plans • Conduct selected follow-up reviews on prior GPRA audits to assess SBA progress and evaluate SBA activities in developing goals and performance measures	As we place increased emphasis in this area, we need to readjust priorities and/or increase resources to accommodate new initiatives. We also need to ensure staff cross training.
Goal 3-Assist SBA in improving its small business development programs	• Participate on Agency teams formed to assess SBA's Business Development program	• Determine the validity of the information being used to report on the government-wide business set aside contracting requirement • Improve data on complaints received in order to conduct trend analysis • Conduct program reviews of entrepreneurial development office • Participate on SBA business development assessment teams	This goal requires that we have greater understanding of program functions, improved data and analytical skills, and that we redirect resources from other areas.
Goal 4-Assist SBA management in identifying and resolving persistent and emerging management issues	• Annually evaluate management challenges and review current and past work to identify new challenges	• Improve intelligence systems by surveying staff on key management issues, formally analyze issues and document results • Enhance follow-up on recommendations • Expand audits of high risk areas	Achieving this goal requires a commitment of time and resources, which may need to be re-allocated from other areas in order to focus on this goal.
Goal 5-Strengthen our ability to identify and have maximum impact on the most significant SBA issues		• Improve timeliness, knowledge management, and internal MIS • Establish intake office to screen requests for information/services	We need to improve our processes and accountability.

SECTION 3 OIG STRATEGIC GOALS, PERFORMANCE MEASURES, AND STRATEGIES

Strategic Goal 1
Prevent fraud and unnecessary losses in SBA programs

Discussion: SBA has a wide range of programs designed to help small businesses gain access to capital, participate in the Federal procurement market, and better plan and manage their operations. Among the services offered, 75 percent of SBA's resources are devoted to credit programs. Chief among these is the Section 7(a) program -- SBA's largest lending program and its primary vehicle for providing small businesses with access to credit. In fiscal year 2001, Section 7(a) loan approvals totaled over 9.8 billion and total outstanding loans totaled over 34.3 billion. The disaster loan program is another key SBA lending program. It is the primary form of Federal assistance for non-farm, individuals and businesses that suffer disaster losses. This program is particularly vulnerable due to the need to expedite processing of disaster loans. In fiscal year 2001 the SBA approved over $1 billion in disaster loans; outstanding disaster loans totaled over $4.6 billion.

To ensure that these and other SBA programs meet their objectives, comply with applicable laws and regulations, and protect the government's assets, appropriate internal controls must be in place. Unfortunately, these programs have had longstanding internal control problems, resulting in fraud and unnecessary losses. Moreover, as previously noted, these programs are being reengineered, creating both greater risks during the transition period as well as the opportunity to ensure that prior control weaknesses are addressed.

Anticipated Outcomes:

Our work in this area is intended to influence the following outcomes:

- Fraud and unnecessary losses are reduced (stratified by types of loans)
- SBA internal control environment is strengthened and appropriately structured

Implementation Strategies:

STRATEGIES FOR ACHIEVING STRATEGIC GOAL 1			
Crosscutting	Auditing	Investigations	Inspection & Evaluation
• Expand outreach with lenders to educate them on how to identify and prevent potential fraud • Establish a "train the trainer" program for SBA program staff to teach them how to detect fraud • Analyze OIG information and work products to identify vulnerabilities, trends, and fraud patterns and convey findings and trends to SBA program officials and other OIG divisions for their use • Obtain and analyze Agency historical data to Identify problems and determine if privatization is truly cost-effective • Work with Agency officials to develop and incorporate fraud indicators in Agency lender reviews	• Screen defaulted loan prior to asset sales to identify possible fraud or improper loan processing by lenders • Analyze data on Section 8(a) participants to identify any abuses that hamper the achievement of intended purpose of the program • Analyze data on non-citizen loans	• Give priority to investigations with broad potential Agency impact vs. those with a large number of potential indictments • Expand use of civil fraud and suspension and debarment process as a deterrent to lenders and lender agents misconduct • Use IG subpoenas rather than grand jury subpoenas to avoid problems using information on civil and administrative cases. • Organize TDY task forces to investigate major cases • Initiate proactive investigations on loan brokers and packagers • Conduct criminal background checks on samples of borrowers who declare no criminal history • Conduct security reviews on all non-citizen borrowers	• Support sampling project • Conduct surveys to determine problems and risks

Strategic Goal 2
Improve the accuracy of and the security over SBA accounting and management information, including performance data

Discussion: Since fiscal year 1999, SBA has received an unqualified opinion on its financial statements. An unqualified opinion signifies that the information contained in the statements is fairly stated. Despite this achievement, SBA has difficulty producing reliable day-to-day financial and management information to support its operations, primarily because of reliance on outdated IT systems that are not integrated. SBA depends on a complex IT environment that includes over 40 mission critical systems running on legacy mainframes and minicomputers. SBA has also had difficulty developing appropriate and reliable performance data to support its implementation of the Government Performance and Results Act.

As previously noted, SBA has ambitious plans to upgrade its systems, including those used for loan monitoring and financial management. This modernization effort is critical to the success of SBA's operations and to reducing operational, data integrity and security risks.

Anticipated Outcomes:

Our work in this area is intended to influence the following outcomes:

- SBA has more effective operations and improved decision-making
- Improved ability to monitor and evaluate SBA performance
- Improved public confidence in SBA's operations

Implementation Strategies:

STRATEGIES FOR ACHIEVING STRATEGIC GOAL 2			
Crosscutting	Auditing	Investigations	Inspection & Evaluation
Issue 1 – IT Systems Development			
• For new systems development, convene divisions to discuss features needed in the systems to protect the integrity of the programs • Performance/ program data	• Participate on selected Agency project teams when new systems are developed	• Conduct background checks on IT contractors both at HQ and in the field	
Issue 2 – Internal MIS: Day-to-Day Program Delivery/Operational Management Information			
	• Select a statistical sample of the most critical data for selected key programs and determine the quality of data used to report on performance results.		• Assist Agency in reviewing performance monitoring of its programs & whether appropriate data is produced by MIS
Issue 3 – Performance Data Monitoring (GPRA)			
	• Follow-up on prior GPRA audits to assess what SBA has done to implement the recommendations		• Evaluate Agency's activities in developing goals and performance measures to fulfill requirements of GPRA, including assessment of performance data quality
Issue 4 – Management/Administrative Accounting Information			
• Review plan in place to convert to e-gov initiative	• Conduct follow-up reviews to assess implementation of additional new financial systems or components to assess whether they support timely reporting and financial information for day to day decision making and other required performance expectations • Conduct annual FS audit		

Strategic Goal 3
Assist SBA in improving its small business development programs

Discussion: SBA offers a range of services including counseling, training, and financial assistance, designed to help small businesses expand. These services are offered through a variety of delivery channels, including Small Business Development Centers, One-Stop Capital Shops, and the Service Corps of Retired Executives. In addition, SBA operates the Section 8(a) program, which was established to help small businesses access the $200 billion Federal procurement market.

As previously discussed, SBA is in the process of reviewing its business development programs, to improve their integration and address changes in the Federal procurement arena. In addition, SBA needs to address specific issues related to the effectiveness and management of the Section 8(a) program, including the equitable distribution of contracting opportunities among Section 8(a) participants, criteria for determining economic disadvantage, and rules for ensuring that Section 8(a) firms do not pass contracts to non-Section 8(a) firms. SBA also needs to improve its ability to measure the success of its government contracting and business development programs and services.

Anticipated Outcomes:

Our work in this area is intended to influence the following outcomes:

- Improved public confidence in SBA's government contracting and business development programs and services
- Improved efficiency and effectiveness in SBA's delivery of entrepreneurial assistance to small businesses

Implementation Strategies:

STRATEGIES FOR ACHIEVING STRATEGIC GOAL 3			
Crosscutting	Auditing	Investigations	Inspection & Evaluation
• Participate in Agency teams formed to assess and improve SBA's Business Development programs • Perform program reviews of services provided by entrepreneurial development office • Assess Agency program reviews	• Conduct a review to determine the validity of the information being used to report on the Government-wide business set-aside contracting requirement • Conduct more audits of business development activities	• Improve data on and analysis of complaints received for the purpose of conducting trend analysis	• Conduct periodic inspections of business development programs • Assist investigations with analysis of data

Strategic Goal 4
Assist SBA management in identifying and resolving persistent and emerging management issues

Discussion: In response to congressional requests and the Reports Consolidation Act of 2000, we annually develop a list of the most serious management challenges facing SBA. Items listed represent areas particularly vulnerable to fraud, waste, error, and mismanagement, or otherwise pose significant risk and generally have been the subject of one or more OIG or GAO reports. Risks are often confirmed by fraud or abuse found by our investigators. One of our key goals over the next 5 years is to help SBA management resolve these issues as quickly and efficiently as possible.

In addition, we must also be able to identify emerging risks and develop strategies for incorporating appropriate action into our audit, investigative and inspection programs. For example, in conjunction with its emphasis on results-based management, the Office of Management and Budget recently established five Government-wide management goals in the areas of:

- Human Capital Management
- Financial Management
- E-Government
- Competitive Sourcing
- Budget and Performance Integration

During the performance period, we will monitor these and other key trend issues and adjust our programs as needed.

Anticipated Outcomes:

Our work in this area is intended to influence the following outcomes:

- Management challenges identified by OIG are addressed and resolved by SBA management
- New risks are identified as they emerge, and resources are devoted to addressing them

Implementation Strategies:

STRATEGIES FOR ACHIEVING STRATEGIC GOAL 4			
Crosscutting	Auditing	Investigations	Inspection & Evaluation
• Periodically survey SBA staff at all levels • Create a mechanism for documenting and communicating issues as they arise (i.e. key issues for later review) • Once a year form a focus group to concentrate on identified issues • Develop potential emerging issues paper • Outreach: Obtain input from trade groups and other stakeholders • Change annual plan to bi-annual plan • Formally follow up on recommendations– devote appropriate resources and analyze actions taken to address root cause of problems – include follow-up results in semi-annual report • Periodically meet with ADA's to discuss outstanding issues • Assess Agency progress on Presidential Management Agenda items	• Conduct audits of high risk SBA activities to identify issues that adversely affect delivery of programs and performance results.	• Provide internal training at annual training conference to focus investigations on identifying serious control weaknesses noted during investigations	• Annual outreach – SBA employees, OIG employees, SBA trade groups

Strategic Goal 5
Strengthen our ability to identify and have maximum impact on the most significant SBA issues

Discussion: By design, our strategic goals are focused on the critical issues facing SBA. To be successful in addressing these goals, however, we must address certain internal management issues that are integral to the implementation of our strategies. Issues regarding human capital, information technology, and the resource allocation process have widespread implications for the successful implementation of our strategies. Consequently, the Office will develop an integrated, consolidated operating plan that reflects the actions that each OIG function will take to support the goals and strategies in this strategic plan. The operating plan will specify more detailed actions that support the strategic goals and will serve as a mechanism for helping to ensure that the entire organization is focused on achieving the same outcomes.

Anticipated Outcomes:

Our work in this area is intended to influence the following outcomes:

- Improved timeliness leading to greater impact
- Greater sharing of information within OIG
- IT investments fully support operations and facilitate communications, data analysis and knowledge management
- Organizational structure that provides best utilization of OIG resources

Implementation Strategies:

STRATEGIES FOR ACHIEVING STRATEGIC GOAL 5					
Crosscutting	**Auditing**	**Investigations**	**Inspection & Evaluation**	**Counsel**	**M&P**
• Strengthen interaction and collaboration • Improve balance of reactive and proactive strategies and activities • Understand our human capital challenges and address our workforce training and development needs • Strengthen the usage of and linkage among our planning, day-to-day operations, budget, and accountability • Analyze organization structure and staffing and make adjustments to maximize our effectiveness and efficiency • Use field strategies to conduct crosscutting reviews • Develop Office-wide MIS system • Identify and implement technology for improving knowledge management • Develop criteria for what we take on • Improve employee accountability • Develop a unified planning process that reports on trends and issues and prescribes how we will focus on them • Improve communication and interaction with SBA Administrator and senior SBA management	• Identify ways to focus in areas that have better potential and opportunity to result in "funds for better use" or "questioned costs" • Identify and dedicate resources to handling internal and outside requests for information, assistance, and other non-traditional audit activity	• Improve OIG intelligence sources • Improve balance among criminal, civil, and administrative cases • Improve information sharing among offices • Refocus investigations from tracking the number of hours per case to the duration of the case • New MIS system that generates real time information	• Improve ability to analyze data sources, detect trends and identify vulnerabilities through statistical methods, data mining and other techniques that allow greater efficiency in providing oversight of SBA programs and operations.	• Provide OIG with timely and quality legal support	• Establish intake function to screen requests for comments on Notices, Standard Operating Procedures, and other items – target review to best source and reduce multiple simultaneous reviews • Assume responsibilities for managing consolidated OIG MIS • Revise semiannual report presentation to include a summary of the SBA situational assessment – status of key issues

SECTION 4 RELATIONSHIP OF THIS STRATEGIC PLAN TO OUR ANNUAL PERFORMANCE PLAN, BUDGET, AND SEMIANNUAL REPORTS TO THE CONGRESS

Our five strategic goals set the strategic direction for the Office and serve as the foundation for other planning and budgeting functions. They are based on the critical issues facing SBA and provide the framework for the audit, inspection, evaluation, investigative, and support activities proposed in OIG annual performance plans and in the more detailed internal operating plan. To establish the required linkage between the general goals and objectives in the strategic plan and the measures in the annual plan, the strategic plan contains high-level outcomes we anticipate will result from our work. The annual performance plan contains the more specific annual performance goals that will measure our progress in meeting our strategic goals. It also provides an understanding of the resources required to implement our strategies and achieve our performance goals.

As required by the IG Act we will report on the results of our audits and investigations semiannually to the Congress. In our semiannual reports we will describe the linkage between our strategic goals and our operations, highlighting progress against our strategic and performance goals.

SECTION 5 KEY EXTERNAL FACTORS

OIG has established objectives and performance measures that are directed toward insuring the quality of the work and customer service we provide to SBA and Congress. Nevertheless, there are a number of factors beyond our control that could affect our achieving the goals and objectives established in this plan.

1. Resources - A significant decrease in personnel or funding resources would adversely affect the achievement of our goals and objectives and increase the risk of loss to the government and, ultimately, to the American taxpayer.

2. Mandatory Requirements - There are a number of statutory requirements which impact our ability to meet workload requirements. In addition to those found in SBA's enabling legislation, these include the Federal Managers' Financial Integrity Act (FMFIA) of 1982, which requires OIG to render opinions on all FMFIA assurance letters; the Chief Financial Officers Act of 1990, which requires OIG to audit financial statements of all accounts and associated activities of each SBA office and activity; the Government Information Security Reform Act, which requires OIG to report on the Agency assessment of its computer security program; and the Freedom of Information and Privacy Acts, which require executive agencies to provide public and individual access to Federal Agency records, subject to certain exemptions and exclusions.

3. Statutory Changes in SBA Programs - Any significant changes in the Agency statutory authority, e.g., the addition of programs, or the repeal or consolidation of programs, could require modification to the goals and objectives in this strategic plan.

4. Agency Control - The implementation of program and system recommendations or improvements is not within OIG control. The ultimate responsibility and authority to make those determinations rests with the Agency management.

5. Judicial and Administrative Proceedings - OIG cannot control the results of judicial or administrative proceedings that may affect the outcomes of OIG efforts. It is also not within our jurisdiction, authority, or responsibility to collect monetary sanctions imposed by the courts or the Agency (restitution, fines, penalties, debts, etc.) as a result of our reviews or investigations.

SECTION 6 PERFORMANCE EVALUATION

While this strategic plan was developed based on SBA's statutory mission and on our responsibilities under the IG Act, we also took into consideration prior OIG audit, inspection, and investigation work, and the results of an OIG customer satisfaction survey on effectiveness and impact.

Evaluating progress in meeting OIG outcomes and performance goals will be a continuous activity. Externally, it will be monitored through customer and stakeholder feedback, and external peer review. The customers and stakeholders of OIG include (1) the Administrator and senior management of SBA, (2) the Congress, especially the Chairmen of the cognizant House and Senate committees and subcommittees, and (3) program participants. We may use surveys of customers and stakeholders as appropriate, as well as meetings and correspondence with them, to determine if we are addressing critical needs or if changes in strategies are necessary. We will also report on the results of our recommendations for systemic improvements by assessing the Agency's implementation actions within 3 years after management decisions (agreement to take specific corrective action) are reached on our reports.

Internally, OIG will track established performance measures in the management information system, use the operating plan quarterly review process, and conduct periodic employee surveys.

SECTION 7 RESOURCES AND OPERATIONAL RESPONSIBILITIES

OIG is composed of the Immediate Office of the Inspector General, and the Auditing, Investigations, Inspection and Evaluation, Counsel, and Management and Policy Divisions. In addition to headquarters staff, OIG currently has audit staff in Atlanta, Dallas, and Los Angeles, and investigative staff in Atlanta, Chicago, Dallas, San Francisco, Denver, Houston, Kansas City, Los Angeles, New York, Philadelphia, Seattle, Syracuse, and Puerto Rico.

The **Auditing Division** performs financial and performance audits of SBA programs to promote their economy, efficiency, and effectiveness. This division performs both internal audits of the Agency's management of programs and external audits of its program participants.

The **Inspection and Evaluation Division** conducts analyses to assess the impact, effectiveness and related performance issues of SBA programs and supporting activities. This division also performs "best practices" studies, management reviews, and client satisfaction surveys to assist SBA in improving its program efficiency and oversight.

The **Investigations Division** conducts financial, program, and personnel investigations involving SBA employees and recipients, and maintains the OIG Fraud Line. The results of these investigations frequently provide the basis for civil or criminal prosecution by the Department of Justice or, as an alternative, administrative action by the Agency. The personnel security branch within this division administers the personnel background and name check program for the Agency.

The **Counsel Division** provides independent legal advice to OIG staff; provides subpoena and litigation assistance for all OIG activities; provides training and guidance to OIG staff on Government-wide ethics and SBA-specific standards of conduct; and processes Freedom of Information/Privacy Act requests relative to OIG activities.

The **Management and Policy Division** supports office operations through internal planning, budget formulation and execution, information resources management, personnel, and other administrative services.

SECTION 8 DATA COLLECTION AND VERIFICATION

Several years ago OIG developed a Management Information System (MIS) for tracking its activities. In FY 1998, OIG began enhancing the MIS by integrating it with other types of software, establishing an Executive Query System that will link all OIG division databases, and making the system secure. As OIG refines its internal performance measurement system, additional improvements and modifications will be made in MIS.

As appropriate, quantitative data will be collected and stored in MIS. Much of the quantitative data proposed has been collected for several years. For some of the measures, baselines will need to be established. Monetary results will be reported at the time of management decision in accordance with OIG legislative requirements. SBA's Office of the Chief Financial Officer tracks actual collections. All qualitative data will be thoroughly documented.

ADD THE FOLLOWING DISPLAY TO THE INSIDE FRONT COVER OF THE NEW SBA-OIG STRATEGIC PLAN

OUR VALUES

The following values characterize the culture of our office and communicate our philosophy in approaching our mission:

Respect for the Individual: We treat all people with respect, including internal and external parties that we interact with during the course of our audits, investigations and inspections. In addition, we recognize that people are our most important resource. The dignity, personal well-being, and professional development of our employees are of paramount importance for accomplishing our mission. We promote a work environment that is free of prejudice and discrimination and we value diversity. We encourage creativity and reward exemplary performance.

Excellence and Effectiveness: We strive to be efficient and results-oriented, taking personal responsibility for the quality of our work. Our activities are designed to provide our stakeholders with the highest possible level of useful, timely, and responsive service.

Professionalism and Integrity: We adhere to the highest standards of ethical behavior. How we achieve results is as important as the results themselves. We promote integrity, credibility, professionalism, and accountability in our employees.

Independence and Objectivity: We maintain the freedom and impartiality necessary to objectively and responsibly perform our mission. We accommodate honest differences of opinion, but do not compromise our principles.

Communication: We strive for an environment of open and honest communication internally and externally. We listen to, learn from, and collaborate with our employees and stakeholders.

Teamwork: We work as a team and challenge our employees to work cooperatively across internal and external organizational boundaries. We involve employees at all levels in developing and continually improving our work processes and encourage responsible risk-taking (e.g., criticism, debate, dissent) as a fundamental principle.

Accountability: We are committed to serving as effective and responsible stewards of the taxpayers' dollars. We believe in providing employees with a clear understanding of what is expected of them and with the guidance needed to perform their tasks. Each individual is responsible for her/his actions. Managers are responsible for ensuring that work is fairly evaluated and appropriately recognized.

Report of the
National Commission on
Restructuring the Internal Revenue Service

June 25, 1997

A Vision for a New IRS

Bob Kerrey
Co-Chair

Rob Portman
Co-Chair

Washington, DC

Introduction

It has been over forty years since Congress and the President have considered significant reforms to the Internal Revenue Service (IRS). With this report, once again there is an historic opportunity to overhaul the IRS and transform it into an efficient, modern, and responsive agency. Because of the vital nature of the institution—the IRS interacts with more citizens than any other government agency or private sector business in America and collects ninety-five percent of the revenue needed to fund the federal government—Congress and the President owe it to the American public to seize this opportunity.

The goal of this Report is to recommend changes to the IRS that will help restore the public's faith in the American tax system. Most American citizens are willing to pay their fair share of taxes; the Commission's recommendations will make it easier for them to do so. No single recommendation will fix the IRS, but taken as a whole, this package sets the stage for an IRS that is fair, efficient, and friendly.

This report is based upon a year of intensive work by the Commission members and the professional staff. The Commission received extensive input from American taxpayers and experts on the IRS and tax system, holding 12 days of public hearings and spending hundreds of hours in private sessions with public and private sector experts, academics, and citizen's groups to review IRS operations and services. In addition to holding three field hearings in Cincinnati, Omaha, and Des Moines, the Commission met privately with over 500 individuals, including senior level and front-line IRS employees across the country.

The Commission also received continuous input from stakeholder groups and congressional representatives, and conducted research and surveys to better understand IRS operations and gauge the American public's view of the IRS. Finally, the Commission reviewed thousands of reports and documents on IRS operations, management, governance, and oversight. The report that follows is the result of this year long effort, and it represents the collective judgment of a strong majority of the Commissioners.

As a guiding principle, the Commission believes that taxpayer satisfaction must become paramount at the new IRS and that the IRS should only initiate contact with a taxpayer if the agency is prepared to devote the resources necessary for a proper and timely resolution of the matter.

Our key recommendations are that:

- Congressional oversight of the IRS should be restructured and coordinated through a new entity which ensures that Members and staff have sufficient information to make informed decisions regarding tax administration and policy.

- Overall responsibility for executive branch governance of the IRS should be placed with a new Board of Directors, accountable to the President and the American people, to provide the expertise and continuity to ensure that the IRS achieves its mission. Board members, including those who have experience running large service organizations, will be appointed by the President and confirmed by the Senate for five year staggered terms. The Department of the Treasury would continue to be responsible for tax policy, and the Board will have no involvement in specific matters in the areas of interpretation or enforcement of the tax laws, procurement, or tax legislation.

- The Commissioner of Internal Revenue should be appointed for a five year term and should be given greater flexibility in hiring, firing, and salary decisions.

- The IRS should receive stable funding for the next three years so that its leaders can undertake the proper planning to rebuild its foundation.

- The IRS must address training, operations, technology, culture, and taxpayer education if the IRS is to operate efficiently and with customer focus.

- The IRS must update its technology and treat taxpayer information as a strategic asset to improve its customer service and compliance functions.

- The IRS must develop a strategic marketing plan to make paperless filing the preferred and most convenient means of filing for the vast majority of filers within the next ten years.

- Additional steps should be taken to improve taxpayers ability to recover damages for wrongful actions by the agency, and significant efforts should be made to protect taxpayers from unnecessary disputes with the IRS before they occur.

- Simplification of the tax law is necessary to reduce taxpayer burden and facilitate improved tax administration.

These key recommendations are all geared toward making the IRS more user friendly. Consolidated congressional oversight, an accountable Board of Directors, and a strengthened IRS Commissioner are necessary structural changes to ensure that good decisions are made, that there are clear lines of accountability, and that the IRS leadership has the continuity and expertise to guide the agency. Without all three of these elements—accountability, continuity, and expertise—along with focus of purpose in one governing entity, a turn around of the agency will be difficult.

Furthermore, a stable budget will allow the IRS leadership to plan and implement operations which will improve taxpayer service and compliance. Advancements in technology will make it easier for the IRS to resolve taxpayer problems quickly, thereby reducing the intrusiveness of the government. The Commission's taxpayer rights provisions will give Americans the ability to

fight back if they feel the IRS is not treating them fairly. Finally, tax simplification will make it easier for citizens to comply with their tax obligations with less intrusion from the IRS.

The sum of these recommendations is to make it easier for citizens to interact with the IRS. The Commission found that there are no isolated solutions and believes an integrated approach will set the stage for a more taxpayer friendly IRS and a tax system which Americans can believe in and trust.

Bob Kerrey	Rob Portman
Ernest J. Dronenburg, Jr.	J. Fred Kubik
Fred T. Goldberg, Jr.	Mark McConaghy
Chuck Grassley	Grover Norquist
Gerry Harkins	Robert Tobias
David Keating	Josh S. Weston

UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON GOVERNMENT REFORM — MINORITY STAFF
SPECIAL INVESTIGATIONS DIVISION
OCTOBER 21, 2004
REVISED JANUARY 7, 2005

THE POLITICIZATION OF INSPECTORS GENERAL

PREPARED FOR

REP. HENRY A. WAXMAN

WWW.DEMOCRATS.REFORM.HOUSE.GOV

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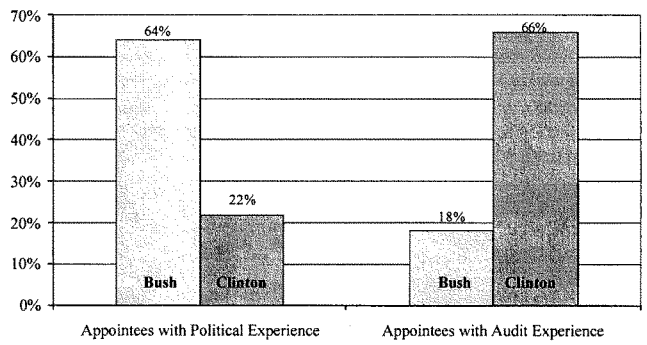
EXECUTIVE SUMMARY

Inspectors General (IGs) are officials within each federal agency who are charged with investigating evidence of waste, fraud, and abuse in the Executive Branch. Over the last 25 years, investigations by IGs have saved taxpayers billions of dollars.

To ensure that IGs are independent and objective, Congress required that they be nonpartisan, specifically directing the President to appoint IGs "without regard to political affiliation." Congress further provided that IGs should be appointed based "solely on the basis of integrity and demonstrated ability" in areas such as accounting and financial analysis.

At the request of Rep. Henry A. Waxman, this report examines the backgrounds of the 43 IGs appointed under the Inspector General Act by Presidents Bush and Clinton over the last 12 years. It finds that IG appointments have become increasingly politicized during the administration of President Bush. Whereas President Clinton typically appointed nonpartisan career public servants as IGs, President Bush has repeatedly chosen individuals with Republican political backgrounds. Over 60% of the IGs appointed by President Bush had prior political experience, such as service in a Republican White House or on a Republican congressional staff, while fewer than 20% had prior audit experience. In contrast, over 60% of the IGs appointed by President Clinton had prior audit experience, while fewer than 25% had prior political experience. Figure 1.

Figure 1: Political versus Audit Experience of Bush and Clinton IGs



Specifically, the report finds:

? Connections to White House: Over one-third of the IGs appointed by President Bush worked in Republican White Houses prior to their appointments as IGs. In contrast, President Clinton appointed no IGs who had worked in any Democratic White House prior to their appointments.

? Other Political Connections: In total, 64% of the IGs appointed by President Bush held some sort of political position, such as a political appointment in a Republican administration or a position with a Republican member of Congress, before their appointments as IGs. Only 22% of the IGs appointed by President Clinton had worked in political positions before their appointments.

? Political Campaign Contributions: Over half of the IGs appointed by President Bush had made contributions to his campaign or other Republican candidates. In comparison, only 25% of the IGs appointed by President Clinton had made any federal campaign contributions.

? Substantive Audit Experience: Only 18% of the IGs appointed by President Bush had previous audit experience, such as experience in an IG's office, at the Government Accountability Office, or at a private accounting firm. In contrast, 66% of IGs appointed by President Clinton had audit experience prior to their appointments.

Prior political experience does not mean that an IG will act in a manner inconsistent with his or her responsibilities. Nonetheless, there have been several high-profile instances of questionable actions by Bush Administration IGs. For example, Janet Rehnquist, the former IG of the Department of Health and Human Services, delayed the release of a critical audit of Florida's pension system until after the reelection of Florida Governor Jeb Bush; Dara Corrigan, Ms. Rehnquist's successor at HHS, refused to investigate whether HHS Secretary Tommy Thompson or White House officials participated in the decision to withhold Medicare cost estimates from Congress; and Lt. Gen. Paul Mikolashek, the U.S. Army IG, reported that the abuses at Abu Ghraib prison were the result of "unauthorized actions taken by a few individuals," not the fault of senior military officials or Defense Secretary Donald Rumsfeld. These actions may be a symptom of the increasing politicization of IGs under President Bush.

I. INTRODUCTION

Inspectors General (IGs) play a critical role in maintaining checks and balances in the federal government: they investigate evidence of waste, fraud, and abuse in federal agencies and report their findings to Congress and the public. Under the Inspector General Act of 1978, they are directed to "conduct, supervise, and coordinate audits and investigations" and to inform the head of the organization and Congress "concerning fraud and other serious problems, abuses, and deficiencies."[1]

According to David M. Walker, the Comptroller General at the Government Accountability Office: "There is no question that the inspector general community has made a significant difference in federal performance and accountability during the past 25 years . . . . [T]hey've saved billions of dollars to the public . . . and they've also had thousands of criminal and civil referrals."[2]

To ensure the independence and objectivity of IGs, the Inspector General Act specifically mandated that the President appoint Inspectors General "without regard to political affiliation" and "solely on the basis of integrity and demonstrated ability" in fields like accounting, auditing, financial analysis, or investigations.[3] Congress also required that IG offices be "independent and objective units" within the agencies they serve.[4] IGs appointed under the 1978 Act require confirmation by the Senate, and they may be removed only if the President communicates to Congress the reasons for the removal.[5]

At the request of Rep. Henry A. Waxman, the ranking member of the Committee on Government Reform, this report assesses the backgrounds of the IGs that have

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1 5 U.S.C. App. § 4.

2 Testimony of Comptroller General David M. Walker before the House Government Reform Committee, Subcommittee on Government Efficiency and Financial Management (Oct. 8, 2003).

3 The Inspector General Act of 1978, as amended, provides: "There shall be at the head of each Office an Inspector General who shall be appointed by the President, by and with the advice and consent of the Senate, without regard to political affiliation and solely on the basis of integrity and demonstrated ability in accounting, auditing, financial analysis, law, management analysis, public administration, or investigations." 5 U.S.C. App. § 3.

4 The Inspector General Act of 1978, as amended, created offices of inspector general within federal agencies "[i]n order to create independent and objective units" to "conduct and supervise audits and investigations," "to prevent and detect fraud and abuse," and "to provide a means for keeping the head of the establishment and the Congress fully and currently informed about problems and deficiencies relating to the administration of such programs and operations and the necessity for and progress of corrective action." *Id.*

5 *Id.*

been appointed over the last 12 years by Presidents Bush and Clinton. It is the first report to examine systematically whether the IGs have in fact been appointed "without regard to political affiliation" and "solely on the basis of integrity and demonstrated ability" as the 1978 law requires.

II. METHODOLOGY

This report analyzes the backgrounds of all IGs appointed by Presidents Bush and Clinton and confirmed by the Senate under the Inspector General Act of 1978. This law applies to the IGs in 28 federal agencies, including all 15 cabinet departments and the major independent agencies.[6] In total, the report examines the backgrounds of 43 IGs, 32 of whom were appointed by President Clinton and 11 of whom were appointed by President Bush. Individuals appointed to more than one IG position by the same President are included only once for statistical calculations.

For each IG, the report examines (1) whether the individual had political experience prior to his or her appointment, (2) whether the individual had made federal political contributions, and (3) whether the individual had prior audit experience. Information on political contributions was obtained through the Center for Responsive Politics website at www.opensecrets.org, which contains records of political contributions from 1989 to the present.

For the purposes of the report, "political experience" means having worked in the White House, having held a political position in a federal agency (except in an IG office), having worked for a member or committee of Congress, having run for federal office, having worked for the Democratic National Committee or Republican National Committee, or having held a political position in state

[6] Under the Inspector General Act of 1978, as amended, IGs nominated by the President and confirmed by the Senate are established in the following agencies: Agency for International Development; Corporation for National and Community Service; Department of Agriculture; Department of Commerce; Department of Defense; Department of Education; Department of Energy; Department of Health and Human Services; Department of Homeland Security; Department of Housing and Urban Development; Department of Interior; Department of Justice; Department of Labor; Department of State and the Broadcasting Board of Governors; Department of Transportation; Department of the Treasury (includes both the Treasury IG and the Treasury Inspector General for Tax Administration); Department of Veterans Affairs; Environmental Protection Agency; Federal Deposit Insurance Corporation; General Services Administration; National Aeronautics and Space Administration; U.S. Nuclear Regulatory Commission; Office of Personnel Management; Railroad Retirement Board; Small Business Administration; Social Security Administration; Tennessee Valley Authority; and Export-Import Bank.

government for either President Bush or President Clinton when they served as governors. A federal agency position is considered "political" if it was listed as such in *United States Government Policy and Supporting Positions* (the "Plum Book"), published alternately by the Senate Committee on Governmental Affairs and the House Committee on Government Reform. For the purposes of this report, "audit experience" means employment in an IG office, at the Government Accountability Office (GAO), or with a private accounting firm.

Information about the backgrounds of the IGs was drawn from publicly available sources, including published profiles, Senate testimony, and government press releases.

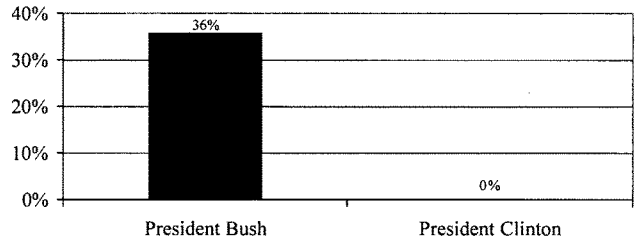
III. FINDINGS

This report finds that the IG appointments of Presidents Bush and Clinton differ markedly. Two-thirds of President Clinton's appointments had prior audit experience, while fewer than one-fourth had prior political experience. These figures are reversed for President Bush's appointments: approximately two-thirds of President Bush's appointments had prior political experience, while fewer than one-fifth had prior audit experience. Whereas President Clinton typically appointed nonpartisan career public servants to IG positions, President Bush has favored individuals with Republican backgrounds in his appointments.

A. Connections to the White House

Over one-third of the IGs appointed by President Bush (36%) worked in a Republican White House prior to their IG appointments. These included senior positions in both the White House of President George W. Bush and the White House of his father, President George H.W. Bush. In contrast, none of the IGs appointed by President Clinton worked in a Democratic White House before his or her appointment. Figure 2.

Figure 2: IG Appointees Who Worked in White House Political Positions



One example of an IG appointed by President Bush with White House experience is Janet Rehnquist, who was appointed Inspector General of the Department of Health and Human Services. Ms. Rehnquist, who is also the daughter of Supreme Court Chief Justice William Rehnquist, served in the first Bush Administration for three years as Associate Counsel to the President. Other examples include Robert W. Cobb, who served as Associate Counsel in the second Bush Administration before his appointment as Inspector General of NASA, and Clark Ervin, who served as Associate Director of Policy in the Office of National Service in the first Bush Administration prior to his appointment as Inspector General of the State Department and later the Department of Homeland Security.

Another example of an IG with White House experience is Stuart Bowen, who was appointed as Inspector General of the Coalition Provisional Authority by President Bush. Prior to his appointment as Inspector General, Mr. Bowen had held numerous positions in President George W. Bush's White House, including Deputy Assistant to the Secretary and Deputy Staff Secretary, and Special Assistant to the President and Associate Counsel. He also served as Deputy Counsel to the Bush-Cheney transition team and was a "key player" in the Florida recount.[7] Although Mr. Bowen is an IG with previous White House experience, he is not included in the tally of Bush Administration IGs because the CPA IG does not technically fall under the Inspector General Act.

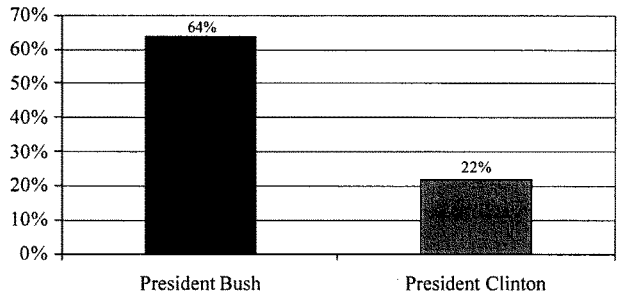
B. Other Political Connections

When other forms of political work experience are considered, the percentage of IGs appointed by President Bush with prior political experience increases to 64%.

[7] *Code Orange: Glowing Lawyer*, Washington Post (Jan. 9, 2004).

In contrast, only 22% of IGs appointed by President Clinton worked in political positions before being appointed. Figure 3.

Figure 3: IG Appointees Who Held Prior Political Jobs



An example of an IG with political experience outside of the White House is Joseph Schmitz, who was appointed as Inspector General of the Department of Defense by President Bush. Prior to his IG appointment, Mr. Schmitz served as Special Assistant in the Office of Attorney General Edwin Meese during the Reagan Administration. Although it does not count as "political experience" under the definition used in this report, Mr. Schmitz also provided legal representation to Republican Speaker of the House Newt Gingrich and the Washington Legal Foundation, a conservative interest group, after leaving the Reagan Administration. Mr. Schmitz is the son of former Republican Representative John G. Schmitz.

Several of the IGs appointed by President Bush had prior political experience working for Republican members of Congress. Before his appointment by President Bush as Inspector General of the General Services Administration (and his pending nomination to be Inspector General of HHS), Daniel Levinson served for three years as Chief of Staff and Counsel to Republican Congressman Bob Barr, who was the first member of Congress to call for the impeachment of President Clinton.[8] Before his appointment by President Bush as Inspector General of the Small Business Administration, Howard Damelin spent several

[8] Mr. Levinson began serving as Acting IG at HHS on October 1, 2004, having been nominated IG of HHS by President Bush in July 2004. He is awaiting Senate confirmation for that position.

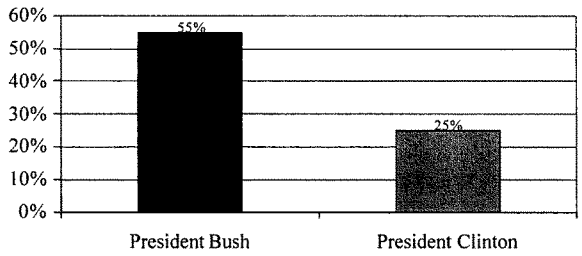
years as Staff Director and Chief Counsel of the Republican staff of the Senate Permanent Subcommittee on Investigations. Mr. Damelin also served as Senior Counsel for Senator Fred Thompson, the Chairman of the Senate Governmental Affairs Committee, during Senator Thompson's investigations of President Clinton for fundraising improprieties during the 1996 election.

An example of an IG with political experience appointed by President Clinton is Eleanor Hill. Prior to her appointment as Defense Department Inspector General in 1995, Ms. Hill worked as Chief Counsel and Staff Director to Senator Sam Nunn, the Chairman of the Governmental Affairs Committee's Permanent Subcommittee on Investigations.

C. Political Campaign Contributions

Over half of President Bush's IG appointments (55%) made political contributions to President Bush or other Republican candidates prior to their appointments. For example, both Mr. Levinson, the Inspector General of the General Services Administration, and Mr. Damelin, the Inspector General of the Small Business Administration, gave $1,000 to President Bush's election campaign. Only 25% of the IGs appointed by President Clinton made federal political contributions. Figure 4.

Figure 4: IG Appointees Who Made Federal Campaign Contributions

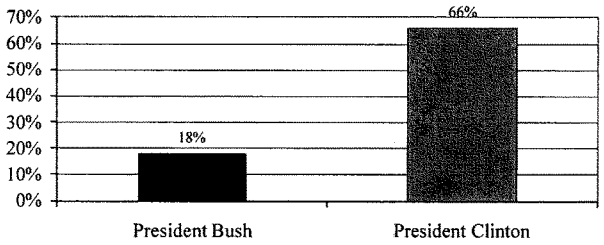


D. Substantive Audit Experience

While approximately two-thirds of the IGs appointed by President Bush had prior political experience, only 18% of IGs appointed by President Bush had previous experience working in an IG's office. No IGs appointed by President Bush had

experience working at GAO or with private accounting firms. In contrast, two-thirds of the IGs appointed by President Clinton had prior audit experience in an IG office, at GAO, or with private audit firms. Figure 5.

Figure 5: IG Appointees with Experience at GAO, OIG, or Private Audit Firms



An example of a Bush appointee with no prior audit experience is Mr. Schmitz, the Inspector General at the Department of Defense. While serving as Inspector General, Mr. Schmitz wrote that he was "neither an accountant nor an auditor by background."[9] Despite this acknowledged lack of auditing experience, Mr. Schmitz was appointed to head the IG office overseeing arguably the most financially dysfunctional agency in the federal government. As the Pentagon IG's website states, "Based on post-Enron independence standards, the Inspector General is the only DoD Officer qualified to issue opinions on the financial statements of the Department of Defense, the annual budget for which exceeds $400 billion."[10]

Of the 11 IGs appointed by President Bush, only two had previous experience at an Inspector General's office. One is John Higgins, the Inspector General of the Department of Education, who worked for six years as Deputy Inspector General in that office before becoming IG.[11] The other is Phyllis Fong, a holdover from

9 Letter from Joseph E. Schmitz to Peter G. Fitzgerald, Chairman of the Subcommittee on Financial Management, the Budget, and International Security, Senate Committee on Governmental Affairs (July 8, 2004)

10 Department of Defense Office of Inspector General website, www.dodig.osg.mil/BIOs/schmitz_bio.htm (Oct. 19, 2004).

11 John Higgins also served as an auditor for the Health Education Welfare Audit Agency from 1968 to 1980 and has worked at the Department of Education Office of Inspector General since 1980.

the Clinton Administration who worked in the IG office at the Small Business Administration (SBA) from 1983 to 1999, at which time President Clinton appointed her Inspector General of SBA. She was appointed IG of the Department of Agriculture by President Bush in 2002.

In contrast, of the 32 IGs appointed by President Clinton, 21 had previous work experience in an IG office, at GAO, or with a private audit firm. For example, Johnnie Frazier worked for 21 years at the Department of Commerce IG office before President Clinton appointed him Inspector General there. Gaston Gianni, Jr., worked for 31 years at GAO before President Clinton appointed him Inspector General of the Federal Deposit Insurance Corporation. Gregory Friedman spent over 20 years at the Department of Energy, including 16 years at the IG office, before being appointed IG of that agency. When President Clinton appointed June Gibbs Brown as IG of HHS, she had previously served as IG at the Department of Interior, NASA, the Department of Defense, and the Navy Pacific Fleet under Presidents Carter, Reagan, and George H.W. Bush.

E. Examples of Questionable Conduct by IGs

Prior political connections do not mean that an individual appointed as an IG will act in a manner inconsistent with his or her official responsibilities. Nonetheless, there have been a number of instances in which the objectivity and independence of IGs appointed during the Bush Administration have been called into question. In some instances, the IGs involved were appointed by President Bush under the Inspector General Act. In other instances, the IGs involved were serving in an acting capacity or served in positions that are not subject to the Inspector General Act. The actions of these IGs raise concerns about whether the politicization of IGs under President Bush is affecting the quality and independence of federal oversight.

Just this week, it was revealed that the Inspector General of the Central Intelligence Agency may be suppressing a critical report on intelligence failures related to the September 11 attacks until after the election. [12] Other examples of questionable conduct include actions taken by the Inspectors General of the Department of Health and Human Services and the Department of Defense.

1. Actions by HHS IGs

One of the first IGs appointed by President Bush was Janet Rehnquist, the daughter of Supreme Court Justice William Rehnquist. Prior to her appointment as Inspector General of the Department of Health and Human Services, she had

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[12] *The 9/11 Secret in the CIA's Back Pocket*, Los Angeles Times (Oct. 19, 2004).

served as Associate Counsel to President George H.W. Bush and Counsel to the Republican staff of the Senate Permanent Subcommittee on Investigations. According to Paul Light of the Brookings Institution, President Bush's appointment of Ms. Rehnquist was intended to send a "dramatic signal" that the Bush Administration did not want a strong Inspector General at HHS.[13]

Questions about Ms. Rehnquist's independence and objectivity arose soon after her appointment. Ms. Rehnquist delayed an audit of Florida's pension system that might have negatively affected Governor Jeb Bush's 2002 election bid after she received a call from Governor Bush's Chief of Staff, Kathleen Shanahan, a former aide to Vice President Cheney.[14] In reviewing Ms. Rehnquist's actions, GAO concluded that she "did not appropriately investigate the implications of her decision before agreeing to delay what ultimately resulted in a report containing significant monetary findings."[15]

In another incident, allegations surfaced that Ms. Rehnquist directed the settlement of a case against a hospital in Pennsylvania after receiving a letter from three members of Congress encouraging her to settle the case quickly. In this matter, GAO concluded that she acted "possibly against the government's financial interest."[16] Within the IG office, Ms. Rehnquist also "initiated a variety of personnel changes in a manner that resulted in the resignation or retirement of a significant portion of senior management, disillusioned a number of higher level OIG officials and other employees and fostered an atmosphere of anxiety and distrust," according to the report by GAO.[17]

Ms. Rehnquist resigned her position in June 2003 "under fire from members of Congress and government investigators for alleged professional misconduct," including whether she had improperly infused politics into her oversight duties.[18]

Ms. Rehnquist was succeeded by Dara Corrigan, who was appointed by Secretary of Health and Human Services Tommy Thompson to serve as the acting IG.[19]

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13 *In the Belly of the Beast*, National Journal (Nov. 1, 2003).

14 U.S. General Accounting Office, *Department of Health and Human Services: Review of the Management of Inspector General Operations* (June 2003) (GAO-03-685); *State Owes U.S. $267 Million, Feds Say*, Miami Herald (Sept. 11, 2003).

15 *Id.*

16 U.S. General Accounting Office, *supra* note 13.

17 *Id.*

18 *Embattled HHS IG Rehnquist To Resign June 1; Hill Critics Alleged Misconduct*, Washington Post (March 5, 2003). *See also A Top Health Official Resigns under Pressure*, New York Times (March 4, 2003); *Delayed Audit Has Bad News for State*, St. Petersburg Times (September 12, 2003).

19 On October 1, 2004, Daniel Levinson replaced Dara Corrigan as acting IG at HHS.

Like Ms. Rehnquist, Ms. Corrigan also received criticism for putting political considerations ahead of her statutory responsibilities. In particular, Ms. Corrigan failed to investigate adequately why estimates of the costs of the controversial Medicare Modernization Act were withheld from members of Congress.

According to the ranking members of five House committees and subcommittees, her investigation into the withholding of the cost estimates was a "superficial recitation of limited facts."[20] The members observed that "[s]ome of the most important issues — such as who knew about the higher cost estimates, when they knew about them and who knew they were being withheld from Congress — were simply not addressed."[21] For example, Ms. Corrigan did not examine whether HHS Secretary Tommy Thompson or White House officials played any role in directing the HHS actuary, Richard Foster, not to share his cost estimates with Democratic members of Congress.

2. Actions by DOD IGs

At the Department of Defense, questions have been raised about the independence and objectivity of Inspector General Joseph Schmitz, who was nominated by President Bush in June 2001. As noted above, Mr. Schmitz had served as a political appointee in the Reagan Administration prior to his appointment. He also provided legal representation to Republican House Speaker Newt Gingrich and the conservative Washington Legal Foundation as a private attorney.

For example, Mr. Schmitz has improperly minimized the significance of Halliburton's overcharges to U.S. taxpayers under contracts for work in Iraq. In July 2004, he stated: "I haven't seen any real deliberate gouging of the American taxpayer, but we are looking."[22] Mr. Schmitz's assertion conflicts with audits by the Defense Contract Audit Agency that found numerous specific instances of overcharging by Halliburton, including a $61 million overcharge for gasoline imported from Kuwait.[23] It also conflicts with congressional testimony from

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20 Letter from Reps. Henry A. Waxman, John D. Dingell, Charles B. Rangel, Pete Stark, and Sherrod Brown to Dara Corrigan, Acting Principal Deputy Inspector General, HHS (July 15, 2004).

21 *Id.*

22 *IRAQ; Pentagon Official Sees No Gouging*, Houston Chronicle, (July 2, 2004).

23 *See, e.g.*, DOD News Briefing (Dec. 11, 2003) (reporting that Halliburton overcharged to import gasoline into Iraq from Kuwait by $61 million through September 30, 2003). *See also* Defense Contract Audit Agency, *Audit Report No. 3311-2004K24020001* (Dec. 31, 2003) (finding significant deficiencies in Halliburton's cost estimating system); Defense Contract Audit Agency, *Status of Brown & Root Services (BRS) Estimating System Internal Controls* (Jan. 13, 2004) (recommending contacting DCAA before entering into future negotiations with Halliburton); Defense Contract Audit Agency, *Audit Report No.*

multiple former Halliburton employees who provided documentation of widespread inflated charges by Halliburton.[24]

In another example, Mr. Schmitz made statements that exonerated senior Pentagon leaders from responsibility for the abuses at Abu Ghraib. After returning from a week-long visit to Iraq in June 2004, Mr. Schmitz stated that abuses at the Abu Ghraib prison appeared to be the fault of a few "bad eggs."[25] Although he did not conduct any substantive investigation of the abuses, Mr. Schmitz stated that he was not "aware of any illegal orders that came from any leaders."[26]

In addition to Mr. Schmitz, who serves as IG for the entire Department of Defense, each of the service branches has its own IG, who is appointed by the head of that military service. The independence and objectivity of one of these IGs, the Inspector General of the Army, Lieutenant General Paul Mikolashek, has also been questioned. General Mikolashek issued a report in July 2004 on the prison abuses at Abu Ghraib, concluding that senior officers were not at fault for the abuses. According to the report, the abuses were "unauthorized actions taken by a few individuals."[27]

These statements were subsequently contradicted by an independent panel headed by former Defense Secretary James R. Schlesinger, which faulted the Pentagon's top civilian and military leadership for allowing the conditions that led to the abuse at the Iraq prison.[28] The findings were also contradicted by a subsequent report by Generals Anthony Jones and George Fay, which criticized senior military officers for "lack of oversight at the facility, failing to respond in a timely manner to reports from the International Committee of the Red Cross, and for issuing policy memos that failed to provide clear, consistent guidance."[29]

3311-2002K11010001 (May 13, 2004) (identifying several deficiencies in Halliburton's billing system and subcontract management).

24 *See* House Committee on Government Reform, *Hearings on Contracting and Rebuilding of Iraq: Part IV* (July 22, 2004); Senate Democratic Policy Committee, *Hearings on Contracting Abuses in Iraq* (Sept. 10, 2004); Senate Democratic Policy Committee, *Hearings on Iraq Contracting Abuses* (Feb. 13, 2004).

25 *Pentagon Inspector General Says Prisoner Abuse in Iraq Done by 'Bad Eggs' in Lower Ranks,* Associated Press (June 25, 2004).

26 *Id.*

27 Department of the Army Inspector General, *Detainee Operations Inspection* (July 21, 2004).

28 Department of Defense, *Final Report of the Independent Panel to Review DOD Detention Operations* (Aug. 23, 2004).

29 Department of the Army, *Investigation of Intelligence Activities at Abu Ghraib* (Aug. 25, 2004).

IV. CONCLUSION

Inspectors General serve a critical oversight function: investigating and preventing waste, fraud, and abuse in executive branch agencies. To ensure their independence, the Inspector General Act of 1978 specifically mandates that the President appoint IGs without regard to political affiliation. Yet despite these requirements, IG appointments have become increasingly politicized under President Bush. Whereas most of the IGs appointed by President Clinton had previously held positions as nonpartisan auditors and few had had prior political experience, approximately two-thirds of the IGs appointed by President Bush had prior political experience and fewer than one-fifth had prior audit experience. This growing politicization of IGs threatens public confidence in the independence and objectivity of the Inspectors General.

APPENDIX: EXPERIENCE OF INSPECTORS GENERAL UNDER PRESIDENTS BUSH AND CLINTON

The following list includes all Inspectors General (IGs) appointed by Presidents Bush and Clinton under the Inspector General Act. For each IG, the list shows White House, political, and audit experience. For the purposes of the report, "political experience" means having worked in the White House, having held a political position in a federal agency (except in an IG office), having worked for a member or committee of Congress, having run for federal office, having worked for the Democratic National Committee or Republican National Committee, or having held a political position in state government for either President Bush or President Clinton when they served as governors. For the purposes of this report, "audit experience" means employment in an IG office, at the Government Accountability Office (GAO), or with a private accounting firm.

BUSH APPOINTEES

Robert W. Cobb (IG, National Aeronautics and Space Administration)
White House Experience: Associate Counsel to the President (2001–2002)
Other Political Experience: none
Audit Experience: none

Harold Damelin (IG, Small Business Administration)
White House Experience: none
Other Political Experience: Staff Director and Chief Counsel for Senate Governmental Affairs Permanent Subcommittee on Investigations and Senior Counsel for Senate Governmental Affairs Committee (1995–1997)
Audit Experience: none

Kenneth M. Donohue, Sr. (IG, Dept. of Housing and Urban Development)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Clark Kent Ervin (IG, Department of Homeland Security) (former IG, Department of State)

White House Experience: Associate Director of Policy, White House Office of National Service (1989–1991)
Other Political Experience: Office of Attorney General of Texas, including Deputy Attorney General, General Counsel, and Director of Administration (1999–2001); Assistant Secretary of State of Texas (1995–1999); ran for Congress in the 29th District of Texas, won Republican primary, lost general election (1992)
Audit Experience: none

Phyllis Fong (IG, U.S. Department of Agriculture)

White House Experience: none
Other Political Experience: none
Audit Experience: Inspector General, Small Business Administration (1999–2002); Office of Inspector General, Small Business Administration (1983–1999), including Assistant Inspector General for Management and Legal Counsel (1994–1999) and Assistant Inspector General for Management and Policy (1988–1994)

J. Russell George (IG, Corporation for National and Community Service)

White House Experience: Associate Director for Policy, White House Office of National Service (1991–1993); Assistant General Counsel, Office of Management and Budget (1990–1991)
Other Political Experience: Staff Director and Chief Counsel, House Committee on Government Reform, Subcommittee on Government Efficiency and Financial Management (1995–2002)
Audit Experience: none

John P. Higgins, Jr. (IG, Department of Education)

White House Experience: none
Other Political Experience: none
Audit Experience: Deputy Inspector General, Department of Education (1996–2002); Office of Inspector General, Department of Education (1980-1996); Health Education Welfare Audit Agency (1968-1980)

Daniel Levinson (former IG, General Services Administration) (recently nominated IG, Department of Health and Human Services)

White House Experience: none
Other Political Experience: Chief of Staff and Counsel to Congressman Bob Barr (1995–1998); Chairman of the U.S. Merit Systems Protection Board (1986–1993)
Audit Experience: none

Richard W. Moore (IG, Tennessee Valley Authority)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Janet Rehnquist (former IG, Department of Health and Human Services)
White House Experience: Associate Counsel to the President (1990–1993)
Other Political Experience: Counsel, Senate Governmental Affairs Permanent Subcommittee on Investigations (1989)
Audit Experience: none

Joseph Schmitz (IG, Department of Defense)
White House Experience: none
Other Political Experience: Special Assistant in the Office of Attorney General Edwin Meese (1987)
Audit Experience: none

CLINTON APPOINTEES

Hubert T. Bell, Jr. (IG, U.S. Nuclear Regulatory Commission)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Marian C. Bennett (former IG, U.S. Information Agency)
White House Experience: none
Other Political Experience: none
Audit Experience: Office of Inspector General, Department of Energy (1981–1983, 1987–1993), including Executive Assistant to Deputy Inspector General and Senior Attorney

Thomas Bloom (former IG, Department of Education)
White House Experience: none
Other Political Experience: CFO and Assistant Secretary for Administration, Commerce Department (1993–1995)
Audit Experience: Partner, Kenneth Leventhal & Co. (1988–1993); Leventhal & Horwath (1984–1985)

Eljay Bowron (former IG, Department of Interior)
White House Experience: none
Other Political Experience: none
Audit Experience: Assistant Comptroller General, Office of Special Investigations, General Accounting Office (1997–1998); Deputy Inspector General, Office of Inspector General, Social Security Administration (1997)

Michael Bromwich (former IG, Department of Justice)
White House Experience: none
Other Political Experience: Assistant to the Attorney General (1993–1994)
Audit Experience: none

Earl E. Devaney (IG, Department of Interior)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Martin J. Dickman (IG, Railroad Retirement Board)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Glenn A. Fine (IG, Department of Justice)
White House Experience: none
Other Political Experience: Counsel, Senate Labor and Human Resources Committee
Audit Experience: Office of Inspector General, Department of Justice (1995–2000), including Director of OIG's Special Investigations and Review Unit (1996) and Special Counsel to the IG (1995)

Phyllis Fong (former IG, Small Business Administration; currently Bush appointee to U.S. Department of Agriculture)
White House Experience: none
Other Political Experience: none
Audit Experience: Inspector General, Small Business Administration (1999–2002); Office of Inspector General, Small Business Administration (1983–1999), including Assistant Inspector General for Management and Legal Counsel (1994–1999) and Assistant Inspector General for Management and Policy (1988–1994)

Johnnie Frazier (IG, Department of Commerce)
White House Experience: none
Other Political Experience: none
Audit Experience: Office of Inspector General, Department of Commerce (1978–1999), including Acting Inspector General (1998–1999) and Assistant Inspector General for Inspections and Program Evaluations (1994–1998)

Gregory H. Friedman (IG, Department of Energy)
White House Experience: none
Other Political Experience: none
Audit Experience: Office of Inspector General, Department of Energy (1982–1998), including Acting Inspector General (1998), Principal Deputy Inspector General (1997–1998), Deputy Inspector General for Audit Services (1994–1997), and Deputy Assistant IG for Audit Operations (1985–1994)

Susan Gaffney (former IG, Department of Housing and Urban Development)
White House Experience: none in a Democratic Administration*
Other Political Experience: none
Audit Experience: Deputy Inspector General, General Services Administration (1987–1990); Assistant Inspector General for Policy, Plans, and Management, Office of Inspector General, General Services Administration (1982–1987); Director of Policy, Plans, and Programs, Office of Inspector General, U.S. Agency for International Development (1979–1982)

Gaston L. Gianni, Jr. (IG, Federal Deposit Insurance Corporation)
White House Experience: none
Other Political Experience: none
Audit Experience: General Accounting Office (1964–1996), including Associate Director, Government Business Operatives/Resolution Trust Corporation Issues (1990–1996)

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* Ms. Gaffney did serve as Acting Assistant Director of the Financial Management Division and Chief of the Management Integrity Branch of the Office of Management and Budget, but she assumed these positions during the administration of President George H.W. Bush and they are not counted here.

June Gibbs Brown (former IG, Department of Health and Human Services)
White House Experience: none
Other Political Experience: none
Audit Experience: Inspector General, Navy's Pacific Fleet (1991–1993); Deputy Inspector General, Navy's Pacific Fleet (1989–1991); Inspector General, Department of Defense (1987–1989); Inspector General, National Aeronautics and Space Administration (1981–1985); Inspector General, Department of Interior (1979–1981)

Richard Griffin (IG, Department of Veterans Affairs)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Roberta Gross (former IG, National Aeronautics and Space Administration)
White House Experience: none
Other Political Experience: none
Audit Experience: Office of Inspector General, Amtrak, including Director of Investigations and Senior Counsel (1990–1995); Acting Inspector General, National Archives and Record Administration (1993)

Gordon S. Heddell (IG, Department of Labor)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Eleanor Hill (former IG, Department of Defense)
White House Experience: none
Other Political Experience: U.S. Senate Governmental Affairs Committee Permanent Subcommittee on Investigations, including Chief Counsel to minority (1995), Chief Counsel and Staff Director (1987–1995), Chief Counsel to minority (1982–1986), and Assistant Counsel (1980–1982); Special Counsel to Senator Nunn (1987)
Audit Experience: none

James G. Huse, Jr. (former IG, Social Security Administration)
White House Experience: none
Other Political Experience: none
Audit Experience: Office of Inspector General, Social Security Administration (1996–1998), including Acting Inspector General, Deputy Inspector General, Assistant Inspector General for Investigations

Luise S. Jordan (former IG, Corporation for National and Community Service)

White House Experience: none
Other Political Experience: none
Audit Experience: Assistant Director in Financial Audit Group, General Accounting Office (1976–1977, 1984–1991); Senior Manager, Office of Government Services, Price Waterhouse; Senior Auditor, Deloitte & Touche

Valerie Lau (former IG, Department of Treasury)

White House Experience: none
Other Political Experience: Director of Policy, Office of Personnel and Management (1993–1994); consultant at Democratic National Committee job counseling center (1993)
Audit Experience: Senior Evaluator, General Accounting Office (1980–1989)

Lorraine Pratte Lewis (former IG, Department of Education)

White House Experience: none
Other Political Experience: General Counsel, Office of Personnel and Management (1993–1999); Senate Governmental Affairs Committee, including General Counsel, Counsel, and Assistant Counsel (1987–1993)
Audit Experience: none

Wilma Lewis (former IG, Department of Interior)

White House Experience: none
Other Political Experience: Associate Solicitor, Division of General Law, Office of the Solicitor, Department of Interior (1993–1995)
Audit Experience: none

Charles C. Masten (former IG, Department of Labor)

White House Experience: none
Other Political Experience: none
Audit Experience: Deputy Inspector General, Labor Department (1991–1993)

Kenneth Mead (IG, Department of Transportation)

White House Experience: none
Other Political Experience: none
Audit Experience: General Accounting Office (1975–1997), including Deputy Assistant Comptroller General for Policy (1996–1997) and Director of Transportation Issues (1987–1995)

Everett L. Mosley (IG, U.S. Agency for International Development)
White House Experience: none
Other Political Experience: none
Audit Experience: Deputy Inspector General, U.S. Agency for International Development (1994–2000); Office of Inspector General, U.S. Department of Agriculture (1969–1994), including Deputy Assistant Inspector General for Audit (1988–1994), and Regional Inspector General for Audit (1980–1988)

George J. Opfer (former IG, Federal Emergency Management Agency)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Jeffrey Rush, Jr. (former IG, Department of Treasury and U.S. Agency for International Development)
White House Experience: none
Other Political Experience: none
Audit Experience: Deputy Assistant Inspector General for Investigations, Office of Inspector General, U.S. Department of Agriculture (1994); Acting Inspector General of Peace Corps (1993–1994); Office of Inspector General, U.S. Department of Agriculture (1971–1993), including Deputy Inspector General for Investigations (1983–1993)

Nikki Tinsley (IG, Environmental Protection Agency)
White House Experience: none
Other Political Experience: none
Audit Experience: Office of Inspector General, Environmental Protection Agency (1990–1997), including Acting Inspector General (1997) and Deputy Inspector General (1995–1996); General Accounting Office, Auditor Evaluator (1976–1982)

Roger C. Viadero (former IG, U.S. Department of Agriculture)
White House Experience: none
Other Political Experience: none
Audit Experience: none

Jacquelyn L. Williams-Bridgers (former IG, Department of State)
White House Experience: none
Other Political Experience: none
Audit Experience: General Accounting Office (1978–1982, 1985–1995); Office of Inspector General, Department of Housing and Urban Development (1983–1984)

David C. Williams (former Treasury IG for Tax Administration, Social Security Administration, Department of Treasury)

White House Experience: none
Other Political Experience: none
Audit Experience: Inspector General, Nuclear Regulatory Commission (1989–1995); Director of Special Investigations, General Accounting Office (1986–1989)

Chair SNOWE. Senator Landrieu.

Senator LANDRIEU. Thank you.

Mr. Thorson, I appreciate the passion in which you've expressed yourself today. I can hear that you bring a lot of emotion to what you do. I've always admired people in that way, that you have a purpose for what you want to do.

It does concern me about some of the past issues Senator Kerry and others have raised. I am very focused from here on because of Katrina and Rita. I'm very fortunate on this Committee to have both leaders, both in the Chair and Ranking Member, who have put this issue of helping the 20,000 businesses that were destroyed by these unprecedented storms and multiple levee breaks.

These businesses would have in many instances survived the hurricane. They couldn't survive the unprecedented number of levee failures that caused the catastrophic flooding of 10 to 12 to 15 feet of water. This is how most of these businesses went out of business, because of a disastrous and somewhat unexpected flood.

Based on the questioning already about your mission to detect and prevent waste and fraud and abuse, I would just add to what both Senator Kerry and the Chairwoman said about also promoting economy, efficiency, and effectiveness. Because the SBA, I mean, is the only thing right now between these businesses being able to get themselves back up and running or literally going out of business and maybe never coming back.

This is about generations of families that have owned these businesses, people that have put all their life savings in these businesses. If this agency doesn't work well, then there are just lots of dreams that are crushed.

That's part of what is the hard thing about us from this position, watching an agency that's on the front line and not able to deliver. We would think that—I would think that the IG, while you want to be focused on fraud and abuse—the real issue is the amount of taxpayer dollars being wasted to no good end, and having businesses that need to generate jobs not able get a hand up.

My question is: Will you commit to give at least the same amount of time, or even a little advantage to the area of inefficiency than on prosecuting the individual potential wrongdoer, as opposed to turning a blind eye to an agency that is maybe falling down on its job to help Americans who need help, if ever they need it now?

Mr. THORSON. Absolutely. Senator Kerry made a good point. He said, "this really isn't mentioned in your statement." And that's true.

Trying to comment on how you're going to improve efficiency in an agency that you've never been in is somewhat difficult. That doesn't mean you're not committed to it, and that doesn't mean that you can't do that, because we can. It does mean that I don't profess to be an expert in a lot of things. I want to—that is a goal. That is something I want to do, and I will do. You framed it as a commitment, and I will make such a commitment to you. I will figure out how to do this and what is lacking and how to best make it better.

Senator LANDRIEU. Would you also commit that if your nomination goes through, within 30 days of your appointment, to go down

to the Gulf Coast and visit not just the areas of New Orleans that are more famous than others, but to actually walk through these neighborhoods where these businesses are destroyed, all along from Pascagoula to Beaumont, Texas, and places in between, to see the destruction of what this unprecedented flooding brought forth?

Mr. THORSON. Earlier I mentioned that I had made a promise to Senator Kerry in a meeting we had about politics. I will make exactly the same kind of promise to you about that. In fact, the truth is, in the months that this nomination has been pending, my wife and I have talked many times about what we would do, and one of the very first things I intend to do is to do exactly as you said.

That's an easy promise to make, and you can count on that.

Senator LANDRIEU. The reason I press that is because every Senator that has come down, every House member that I know of, has come back and called my office and said to me—not everyone has called, but everyone that has called has said this. They've said, "Senator, no matter how many times I've heard you and Senator Vitter speak, I could not believe what I saw."

Again, it's because it wasn't just the hurricane. We've seen hurricanes. We've seen earthquakes. We've seen the disaster. What we've never seen is a catastrophic flood, like Noah's Ark. I mean, that's what people have to get in their mind. It was like Noah's Ark. I mean, and when the water goes away after 40 days in that case, or in our case 2 weeks, it's just unbelievable the devastation.

You can look at a map. That's why when people say, "we don't have enough, we can't verify if the business really went out of business," you don't need to do anything other than to look at a map. If they were located anywhere around a certain neighborhood, there is a 100-percent chance that they couldn't survive.

It's not like a regular hurricane, where some businesses survive and some don't. I mean, you have to be concerned somebody might apply for a loan. They didn't have a shingle removed from their roof, and they got in anyway. In this case, if you were in this zip code or in this neighborhood, there was no chance that you were not flooded with 15 feet of water. Just go ahead and move the system a lot faster.

That's what we're trying to get these agencies in Washington to understand: Not asking for special favor or more money, but just understanding that the nature of the disaster was different. That is what we're having a hard time convincing people of.

Mr. THORSON. I was asked earlier about lessons that I had learned doing this kind of work, and it fits right into what you were just saying. One of the things that I really believed in when I was doing hearings and Senate investigations was listening to the real people. You had real people—and that meant we had real IRS people testify. In one case, we had a real Mafia hood testify. Because nothing gets it across as much as talking to real people.

That's true, whether it's you all listening to them, or the cameras or whatever. But it makes it real. When you're talking about the things that you want to do and passing legislation, these are who it affects. These are the people who—what you're talking about is exactly the same thing.

The reason that I felt so strongly from day one when we were talking about an IG of SBA and seeing—I did not understand, I'll

be honest with you. In the very beginning, I did not know that disaster relief loans went through SBA. I learned that pretty quick.

You've got to do that. You have to go down there and see it and talk to people and understand the real people. That is one similarity that is exactly the same because you'll never get a feel for it. I think anybody who's listened to me knows I pretty much get into my job. It's a very important part of my life. I will do that.

[The prepared statement of Senator Landrieu follows:]

Statement of Senator Mary L. Landrieu
for Small Business Committee Hearing on
Small Business Administration Inspector General Nominee
Eric M. Thorson

Introduction

Thank you Madam Chair for giving us the opportunity to hear from Mr. Thorson. Also thank you Chairman Grassley for your introduction of this nominee.

Welcome to you Mr. Thorson and let me thank you for your testimony here today. I want to commend you for your background and experience, especially your service to our country in Vietnam. I was pleased to see that you have personal experience with the Small Business Administration (SBA) and that you recognize its importance to small businesses. It's a good thing that you repaid the SBA loan you received in full - if you had not, it would have made for an interesting hearing today!

The SBA Inspector General plays an important role in keeping the SBA Administrator and Congress, fully informed about how the SBA is operating and whether there are any problems with its operations. The IG also recommends corrective actions and monitors progress in the implementation of these actions, in addition to the IG's auditing, inspection, and investigation responsibilities to prevent fraud and abuse.

SBA and Gulf Coast Recovery

We especially need a strong person in the IG position in the wake of Hurricane Katrina. Katrina was not a normal hurricane, we all know that. In Louisiana, over 18,700 businesses were catastrophically destroyed and 365,200 residents were left homeless as a result of these hurricanes. SBA will be the key, in these coming years, to helping our people rebuild.

Despite the important role that SBA will play, I have not been impressed with SBA's performance so far. Immediately after the storm, SBA did not have enough staff on the ground to do damage assessments. There were problems with SBA's loss verification software that caused lengthy delays. Today, loan approvals are taking 80 days. Loan closings take another 25 days. Just a few weeks ago, we learned that the Disaster Loan program was going to run out of money unless Congress passed emergency funding for the program.

Administrator Barreto has called Katrina an "unprecedented disaster" and said that the SBA was providing an "unprecedented response." My constituents have told me that the SBA's response has been 'unprecedented' for its slowness and mismanagement.

SBA Disaster Loan Program Management

According to your prepared statement, the only issue that you mention pursuing is investigating disaster loan fraud in the Gulf. Certainly we have to stop fraud. However, I am

disturbed by the implication that people who are experiencing unprecedented suffering will make "unprecedented" attempts to cheat the government, as you state in your testimony.

I cannot tell you the number of people whom I know that have applied to SBA for disaster loans. People have lost everything down there. They are not thinking about how to cheat the government, they are trying to rebuild their lives. If you are confirmed, I encourage you to go to the Gulf - to Gulfport and to New Orleans - take a look at the houses and businesses that were destroyed, talk to the people down there.

As you examine the Disaster Loan Program, I strongly suggest that you set your sights a little closer to home: to the SBA itself here in Washington. Nothing can be more fraudulent than a government agency that has failed the taxpayers. I challenge you to take on the more important task of investigating how the SBA has let down business owners and residents in the Gulf.

As I mentioned, the Disaster Loan Program came close to running out of money toward the end of January. SBA had to get approval from Congress to reprogram $100 million so that the program could operate for another two weeks. Congress then had to pass an emergency appropriation to reallocate $712 million from FEMA to SBA in order to keep the disaster loans coming through the end of April. I certainly supported this legislation, but I am alarmed that Congress has been put in this position by SBA.

As I understand it, the problem occurred because the average loan size for Katrina was double what SBA had originally experienced in past hurricanes. The average loan size had been $32,000; the loan size for Katrina is approximately $69,000.

Given that the average loan size for Katrina has been more than $50,000 from day one, I do not see how the agency could come so close to running out of money. The SBA knew how many loan applications they had received, how many they were approving, and it must have known that the average loan size was double very early on. We receive daily reports with this information. Yet despite all of this and Administrator Barreto's promises at hearing before this Committee for an unprecedented SBA response, SBA did not readjust its budgeting for the program earlier on. That is the kind of mismanagement that defrauds tax payers and the people who need this program and I believe that you should examine as Inspector General.

As some of you know, the damage from Katrina was caused not so much by the wind and the rain, but more so from the flood of water resulting from numerous levee breaks. Some have characterized these floods as being similar to Noah's flood in the Bible. What made this flood so heartbreaking was that it resulted from underfunded levees. This was one example of government failing its citizens. SBA is another. Its poor management and deployment in the Gulf is unacceptable. Notifying Congress 13 days before disaster loans in the Gulf are about to run out of funds is unacceptable. That does not provide me or my constituents with any level of certainty or faith in the SBA's ability.

As Inspector General you will be expected, both by this Senator from Louisiana, as well as by my constituents, to ensure that the SBA is efficient, responsible, and responsive to the needs of businesses and homeowners. If its record in the Gulf is any indication, you have a lot of work ahead of you Mr. Thorson.

I thank the Chair and ask that my full statement be submitted for the record.

Chair SNOWE. Thank you, Senator Landrieu.

I just wanted to follow up on a couple of issues with respect to some of the issues that Senator Kerry raised because it was important, as part of the Committee's responsibilities, to examine a number of the issues regarding the IRS investigation that you led on behalf of Chairman Roth and the Senate Finance Committee.

It's our goal to obviously conduct these hearings in a transparent fashion. We had a chance to review a number of the issues, including the GAO report. I just thought it would be important for the record, based on my staff's examination. I want to include this in the record.

When the GAO issued two reports on the claims made with respect to the hearings that you helped to facilitate, it confirmed facts alleged by the witnesses across 10 different categories of factual allegations, including: zeroing out of tax assessments in the manager's unlimited discretion to zero out taxes; the inability of the IRS to oversee zero-out decisions; the perception of favoritism for former IRS executives who now practice before their former IRS colleagues; illegal use of enforcement statistics for performance evaluation of IRS offices; the workplace practices which promoted a climate of racial discrimination within the IRS; the closure of approximately 100,000 tax cases which lacked proper procedures and fair treatment; the abuses of public office for private gain by IRS officials; the substantial difference in the way IRS imposes discipline on its personnel and executives; the inability of the IRS to track allegations of reprisals against employees and taxpayers; and the property damage and fear of intimidation experienced by some taxpayers or their associates during IRS enforcement operations.

In instances, obviously, it was a matter—not that anything was improper, but there was a disagreement in terms of the interpretation of the laws. In some cases, witnesses were mistaken on some points of fact concerning management misconduct and the application of laws and procedures. The GAO also found that two witnesses, who testified of being intimidated by the IRS in a Federal court, found IRS employees misrepresented information in order to search warrants.

I think that across the board on what you were attempting to do as an investigator, your role was obviously to help the Congress in examining how the Internal Revenue Service was administering its responsibilities, and to obviously highlight for the public the problems in the administration of their obligations and responsibilities to the taxpayer.

I thought it was very important to highlight that. We did a very thorough examination, and what we found was nothing improper. It was a disagreement on the law, a very difficult area. It was clear from Chairman Roth's book that he really insisted on being fair; and the fact also that hands were tied, I gather, in terms of being able to have the IRS come before the Committee with its own testimony, as I understand it.

Chairman Roth indicated that Section 6103 had not been used before. Is that correct?

Mr. THORSON. I really can't say. 6103 is the protection of taxpayer information as privileged, and only the Chairman of Finance

and the Chairman of House Ways and Means have that authority. I really don't know when that might have been done before.

Chair SNOWE. Yes. He indicated that in his book, as a matter of fact. In fact, he said—he mentions that in one of the pieces in his book with respect to that.

I think the point is here that obviously these—I think when we're pursuing investigations, it becomes obviously very difficult. We appreciate what you've done. Hopefully you'll learn from some of these issues as well as you go forward.

I think clearly the Small Business Administration—it becomes equally evident that there are a number of issues that will require your aggressive pursuit in examining. Another area is the STAR loan program that was created in the aftermath of 9/11 that began in 2002 and ended in 2003 to help businesses that were adversely affected by the economic impact. We discovered recently, we had an examination done by the Inspector General's office: 85 percent of those loans that were issued, they were unable to determine the eligibility, verifying the eligibility for such loans.

How would you approach a program of this nature in the future to prevent—the question here is, first, either to anticipate, in the instance of disaster loans, when you see a disaster imminent, knowing that the SBA is going to have to be positioned to respond to that, so you prevent certain problems that ultimately developed, as we learned in the last few months, with the administration of these programs by the SBA, the disaster loan programs.

Then, secondly, how do you ensure that in the future, that you also prevent these types of problems and abuses in the administration of a program like the STAR loan? What would you recommend?

Mr. THORSON. Well, in the first instance, these 9/11 loans or STAR loans or whatever, one of the things that I believe should have been anticipated was perception of what was happening here. When you create—when you put together a program, one of the things that you could anticipate, or I believe maybe should have been anticipated, was the fact that when banks were—what is the motivation, first of all? Well, banks had a reduced fee on that where they were going to make more profit.

If you've created a situation where banks are going to make more profit by using these types of loans, you can bet that's what's going to happen. That's exactly what did happen. I believe there was a perfume store in St. Croix, et cetera.

One of the reports that I read was that this was all done and it was perfectly proper, that these loans all fit whatever the policy was. That's a particular part of what an IG does, is measure against those policies. And based on what I've seen, I can't argue that that may have been true.

What happens is when you see it show up on the CBS evening news and it becomes sort of a joke or something, you need to be able to realize that and anticipate that going forward. I guess maybe one of the things, too, that I would say is that my experience up here would lend me to be able to do that because we dealt a lot with those kind of issues.

You have to understand what the goal is first as to what you are trying to do with those loans. Then did what happened meet that

goal? I think what you're saying is no, it did not, because we didn't intend to fund perfume stores in St. Croix.

One of the things that I would like to be able to do is to look at those things while they're either being done or immediately afterwards, whichever is applicable, and to be able to point that out, which in this case I truly believe I would have been able to, and say, "you've got a huge hole here." This is—you have created a profit-making situation that's going to get you in trouble. Then work with the Administrator on how to close those loops so that what you want is to get it to the people who need it and who were entitled to it, and not have the disaster that it kind of resulted in.

Chair SNOWE. Well, with respect to the STAR loan program, it was just a lack of guidance and instructions, vague directions that made it all the more difficult, particularly for the lenders, that ultimately developed into this major problem.

I think that it would be important to review many of these programs and to see exactly what the eligibility guidelines are in many of these programs. Because I think that that is clear; the lack of communication between the Agency and the lenders involved, and what can be done to ensure that we issue the proper guidelines and guidance and instructions with these programs so that abuse or fraud doesn't arise as a result.

That's what happened in this instance, regrettably, because there was no way to determine the eligibility, I gather, from the loan files when they were reviewing them.

Mr. THORSON. Well, I think this comes back again to the idea of being a little more proactive and to be able to get involved on the front end of these things so that you can—because among other things, it gives you the opportunity to work together with the Agency and the Administrator to point out where you think, based on the experience you have, that you're heading for a problem here. In this case, I think it would have been relatively easy to determine.

Chair SNOWE. Absolutely.

Mr. THORSON. The incentive here was pretty clear, and therefore you knew what the banks were going to do. They were going to do as many of these as they could possibly do because they made more profit. That's a pretty simple analysis of it, and that's exactly what happened.

Chair SNOWE. The 85 percent, I think that's an indication of the depth of the problem that obviously something was terribly wrong.

Mr. THORSON. Exactly.

Chair SNOWE. The SBA has also failed to accurately predict disaster loan volumes. That's the other issue. We've had to get additional funding through a supplemental because they neglected to anticipate, to identify, not necessarily precisely but within range of what would be required with respect to these recent disasters.

Unfortunately, we've had to go forward and approve $712 in supplemental funds. The SBA could not even predict the situation in December and early in the month of January. It's only in the last few weeks that they finally realized that they would need this additional funding, and so we've had to provide it. In the meantime, those who depend on these programs had to wait in order to ensure

that there were sufficient funds to go forward with additional loans.

It's the unevenness as well. What I've learned, I think, in the last few months with respect to how the Small Business Administration operates, it's not only the failure to predict, to anticipate, or to prevent serious problems. It's the lack of efficiency in the administration of these programs.

We've heard it's an unprecedented crisis. That requires an unprecedented response. Therefore, I think that the SBA has to be positioned to meet the challenges irrespective of when they occur.

Mr. THORSON. Each of you, I believe, have discussed the idea and used the word "efficiency." That really is maybe one of the most difficult parts of doing the work of an IG, which is to be able to look at an agency and tell an agency how they can make themselves more efficient, how they can do things better. I think that's a natural source of friction when you are telling the head of an agency how he can better run his agency.

Where that's necessary and where we have developed—and I say "we" as the IGs, the real pros that do this kind of thing—that is not a problem in being able to do that. The real work there is to be able to identify those things and to be able to make constructive suggestions as to how to make it more efficient.

It's easy to talk about fraud and stuff, which is why I had it in my opening statement. It's a lot more difficult to be able to assess an agency and to be able to point to places where the efficiencies can be improved, and make recommendations on how to fix it. To say, "here's how we suggest you can do it."

Chair SNOWE. Absolutely.

Mr. THORSON. It is absolutely important.

Chair SNOWE. It is critical, and I think all the more so given the previous track record and experiences, unfortunate examples of what we need to do to improve in the delivery of these programs, not only for the present time but also in the future.

We still have a lot of work to be done in order to complete this process in response to the hurricanes of last fall. We still have a long ways to go.

Mr. THORSON. Yes, ma'am.

Chair SNOWE. Many people are depending on these programs to rebuild the economies and rebuild their homes. I think that's going to be an important contribution in your role as Inspector General. I think it's an excellent idea about the fact of you going down there and being on the ground and being able to do that.

Our staff went down there last fall because I insisted on it to see exactly what was going on and what was going wrong. We quickly realized many of the challenges that the SBA was facing, and it was obviously additional personnel, additional resources, more computers, loan verifiers, and auditors.

Mr. THORSON. A physical presence is important for many reasons. It's important to the people who are on the receiving end of these loans and that have experienced the disaster. It's also important from a leadership point of view for your own group.

That's why I said early on as we talked about the need for the IG to be there and to see that. You're also sending a message to the people that work for you, that this is important and this is how

it's got to be done. I truly believe that. That isn't for any other reason than for that. But it is absolutely true.

The people in the IG office need to know that I will be there. They are also going to be there. We're going to be there a long time. This isn't something that's going to get solved in the next 60 days or something. This is going to be a long time.

Hurricane season starts again in June. It's not going to take much to cause trouble in this area all over again. We need to be there when this happens, and we need to be right there at the forefront, and for many reasons. The fraud is only one part of it.

Chair SNOWE. Well, I appreciate it, Mr. Thorson. I want to thank you for testifying here today. I know that your investigative experience both within the executive and legislative branch will go a long way in helping to make the SBA and our Government more accountable in spending the taxpayers' dollars wisely and efficiently.

I appreciate your testimony this afternoon, and the record will remain open for 2 days, until March 3rd. Additionally, any written requests for Mr. Thorson will be submitted to the Committee by noon on Friday, March 3rd. We also will forward them to Mr. Thorson, and any time that you have a response to any of the questions that are submitted to the Committee, we hope that you could include them for the record by March 9th.

Again, I want to thank you, Mr. Thorson. I'm looking forward to working with you in the future.

Mr. THORSON. Thank you.

Chair SNOWE. This hearing will be adjourned.

[Whereupon, at 3:34 p.m., the Committee was adjourned.]

Senator Olympia J. Snowe
Chair, Senate Committee on Small Business and Entrepreneurship
"Nomination of Eric Thorson to be Inspector General of the Small Business Administration"
March 1, 2006

Opening Statement

Good afternoon and welcome to today's hearing to consider the President's nomination of Mr. Eric Thorson to be the next Inspector General (IG) for the Small Business Administration (SBA). Mr. Thorson, I see that you are accompanied by your family – your wife Susan and your father-in-law Arthur White -- and we welcome them to the Committee.

I also welcome Senator Kerry, and thank him for working with me on this nomination and hearing. And I appreciate my colleague, Senator Grassley, for his presence here as well. Senator Grassley, will be introducing Mr. Thorson, who previously served as Chief Investigator for the Senate Finance Committee.

We come to this hearing at a time when the IG's role at SBA will be *all the more critical*, given the enormous challenges the Agency has faced – and continues to confront – in areas such as the disaster loan program's operation and the unacceptable response to Katrina and Rita, enforcement of government-wide small business contracting rules, and oversight of SBA lending programs. Therefore, it is *imperative* the new Inspector General be aggressive and tireless – as the unprecedented challenges require unprecedented *responses*. So, Mr. Thorson, I look forward to hearing your testimony and to further explore your qualifications to carry out the Inspector General at this pivotal juncture for America's 25 million small businesses and

their employees.

Mr. Thorson certainly brings a depth and breadth of experience – from having served, among other roles, as Director of Defense Issues for the Legislation and National Security Subcommittee of the House Goverment Operations Subcommittee...Chief Investigator for the Permanent Subcommittee on Investigations of the Senate Committee on Governmental Affairs, and for the Senate Committee on Finance...and Special Assistant to Senate Republican leader Trent Lott on corporate fraud investigations.

His past investigative subjects include such major issues as Enron and WorldCom. And he worked in both the executive and legislative branches under Republicans *and* Democrats, including Rep. John Conyers, the late Senator Bill Roth, and – as I mentioned – then-Majority Leader Trent Lott, during his many years of investigative experience. *Moreover*, he has firsthand knowledge of the trials, challenges, and gratification of being a small business owner, who fulfilled his dream with the help of an SBA veteran's loan.

Indeed, we have an obligation to ensure that the person confirmed as the SBA's Inspector General is not only a well-qualified investigator. They must *also* show *passion* in identifying barriers that may limit the success and entrepreneurial spirit of our small businesses, that form the very foundation of the nation's economic growth and job creation potential – having created about three-quarters of all net new jobs annually.

In that light, the Inspector General's office recently began an investigation of the SBA's woeful response to Hurricanes Katrina and Rita, an area I have also investigated at length. As we have learned, the Agency's Disaster Credit Management System was incapable of handling the high

volume of disaster loan applications – nearly 350,000 have been received so far -- and the SBA failed to accurately monitor its disaster financial information and to implement its disaster transformation workforce strategy. This tragic response to a tragic and devastating disaster *must not be repeated* – and the Inspector General will be *key* in determining how we can ensure such bureaucratic lethargy never reoccurs at the SBA.

Mr. Thorson, you will also bear the responsibility of determining whether SBA's administrative procedures measure up to the expectations of America's small business owners. We've seen what *cannot* happen under the Inspector General's watch with the STAR loan program – epitomized by the Inspector General's December 2005 report finding that eligibility could *still* not be determined for 85 percent of the loans reviewed. And the series of ongoing investigations on the effectiveness of the SBA's Lender Monitoring System (LMS) – which is used to provide oversight of lenders and of SBA's handling of lending programs such as the 7(a) and 504 business loans – *further* underscores the Inspector General's vital part in providing aggressive oversight and minimizing abuses of the system.

Similarly, given recent discoveries of small businesses losing prime contracting opportunities to large businesses due to poor oversight of contracting laws, it is fitting that you will bring to this appointment 12 years of experience in successfully investigating and reforming Federal contracting programs. Uncovering, monitoring, and correcting abuses...lax implementation of laws...or waste, fraud, and abuse of taxpayer funds will require your urgent attention, Mr. Thorson, and with your success it will be America's small businesses that reap the *greatest reward.*

Finally, let me say that, obviously, this hearing had been delayed to

provide additional time to thoroughly examine documents pertaining to the 1997 and 1998 hearings on IRS abuses held by the Finance Committee, where Mr. Thorson was Chief Investigator. As the record shows, these hearings led to the enactment of the IRS Restructuring and Reform Act that we passed 96 to 2 in 1998. During this additional time-period, we have further analyzed Mr. Thorson's role in these hearings and interviewed several witnesses, including officials of the Government Accountability Office. Nevertheless, I welcome this opportunity to gain further clarification from the nominee on this particular matter, as well as any other that will impact the SBA and America's small businesses.

I now recognize Senator Kerry for an opening statement.

-Opening Statement for Senator Thune-
Nomination of Eric Thorson
To be Inspector General of the SBA

Madame Chair, members of the Committee- I would like to thank Mr. Thorson for coming before the Committee today. After looking over his statement and his biography, it is clear that he has a heart for public service. He has devoted a large part of his adult life to making government work more efficiently and to exposing those parts of our government that need exposing so that they can be improved.

As the saying goes, sunshine is the best disinfectant, and Mr. Thorson has used that disinfectant many times throughout his career. As most of you all are aware Mr. Thorson is extremely familiar with Congressional hearings, although I can't say that he has ever been in the seat he is sitting in now. Mr. Thorson led the staff work on Senator Roth's investigations and hearings into the IRS, Medicare fraud, and defense contracting. He exposed fraud and inefficiencies that improved our government and helped saved hard-earned tax dollars. This experience will serve him well at the Small Business Administration.

I am also pleased to see here that he has been on the other side of an SBA loan transaction. That is, he has used an SBA loan to start a small aviation business. Having been a younger veteran, looking to start a new career Mr. Thorson used the SBA to jumpstart that career. This experience will greatly serve him in his new capacity inside that same agency.

It is my hope he remembers that experience and the millions of other Americans who are trying to pursue the dream of owning their own business as he works to root out fraud when it has occurred at SBA and prevent it from happening as well.

Thank you again Mr. Thorson for coming before the Committee today and I look forward to supporting your nomination.

United States
Office of
Personnel Management

Federal Investigative Services Division
Federal Investigations Processing Center
Boyers, Pennsylvania 16018-0618

In Reply Refer To: Your Reference:

February 27, 2006

The Honorable Olympia J. Snowe
United States Senator
Chair
Committee on Small Business and Entrepreneurship
428A Russell Senate Office Building
Washington, DC 20510

Dear Senator Snowe:

Mr. Eric Thorson, who is currently under consideration for Inspector General with the Small Business Administration, asked that I submit this letter of reference concerning his current employment with the Office of Personnel Management (OPM). Mr. Thorson has served as a Senior Advisor to the Director of OPM for Investigative Operations and Agency Planning since March 2003.

Mr. Thorson's primary responsibility has been to provide critical leadership for operational components of OPM during the transfer of the Department of Defense's (DoD) personnel security investigations program to OPM. This transfer was successfully completed in February 2005. In total, approximately 1,800 staff and an annual workload of over 800,000 new requests for investigation transferred to OPM. This transfer was an essential step toward fixing long-standing problems in this vital program, helping to ensure our national security and the integrity of the Federal workforce.

Mr. Thorson personally attended to the details of the formal memorandum of agreement between DoD and OPM, as well as many of the financial issues related to the transfer. With his assistance, the transition of this national security program from DoD to OPM was successful.

Mr. Thorson has proven himself to be a man of intelligence, honor, and integrity. His example serves as a model for all of us who work with him, and his tenure at OPM has been marked with excellence.

Sincerely,

Kathy L. Dillaman

Kathy L. Dillaman
Associate Director
Federal Investigative Services Division

CON 132-48-9
November 2003

HALT *An Organization Of*
AMERICANS FOR LEGAL REFORM

February 22, 2006

James C. Turner
Executive Director

Senator Olympia J. Snowe, Chair
Senator John F. Kerry, Ranking Minority Member
Committee on Small Business and Entrepreneurship
428A Russell Senate Office Building
Washington, DC 20510

re: Nomination of Eric M. Thorson

Dear Senator Snowe and Senator Kerry:

I write to enthusiastically endorse the nomination of Eric M. Thorson to the post of Inspector General of the Small Business Administration and to share my personal knowledge about his eminent qualifications and suitability for this position.

From 1990 through 1994, first as Counsel and then as Staff Director of the Legislation and National Security Subcommittee of the U.S. House of Representatives Committee on Government Operations, I worked on a daily basis with Mr. Thorson in directing our oversight activities with respect to the Department of Defense.

The subject matter of these investigations was often complex, ranging from procurement irregularities in the Navy's A-12 aircraft program to mismanagement in the Air Force C-17 Airlifter and DoD's MILSTAR satellite programs. In every investigation, Mr. Thorson fully mastered the technically difficult issues, skillfully assembled and analyzed the evidence, and forcefully presented the need for appropriate remedial action.

During this time he was the consummate professional, who aggressively investigated fraud, waste and abuse in major military programs in a completely nonpartisan manner. Whether working with our Chairman, John Conyers, or with our Ranking Member, Christopher Shays, Mr. Thorson's only concern was uncovering the truth.

I believe that his unique set of skills and experience, coupled with his steadfast refusal to be drawn into partisan controversies, will allow Mr. Thorson to be an extraordinarily effective Inspector General. Please have your staff contact me if you would like to discuss Mr. Thorson's nomination.

Sincerely,

James C. Turner

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NAACP Federal Sector Task Force

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EEO Program About FSTF Members Goals

The Task Force wishes to thank U.S. Senator William Roth, Jr., Chairman of the Senate Finance committee for the superb personal leadership shown during the September 1997 and April 1998 investigative oversight hearings into the operations of the Internal Revenue Service (IRS). We are very appreciative that Senator Roth allowed the NAACP to testify before the Senate Finance Committee to discuss our concerns regarding discrimination practices which were documented as an extremely serious problem for many IRS employees. We should also thank Eric Thorson the former Chief Investigator for the Senate Finance Committee for his support and assistance. The EEOC enforcement power against the various Federal agencies can best be described as minuscule. The ability of the EEOC to order Federal agencies to take corrective action is very limited and mostly ineffective. The lack of strong enforcement power is a serious problem hindering the EEOC in correcting many of the illegal activities that occur. We expect the US President and Congress to take a proactive lead in this fight. Legislation and Executive Orders designed to clean up the EEO are needed now. The final authority over the EEO program must rest in the hands of someone other than the agencies and officials who are being charged with employment discrimination.

Senator Olympia J. Snowe, Chair
Senator John F. Kerry, Ranking Minority
Committee on Small Business and Entrepreneurship
428A Russell Senate Office Building
Washington, DC 20510

February 22, 2006

Dear Senators Snowe and Kerry,

This letter is in support of Mr. Eric Thorson's nomination for Inspector General of the Small Business Administration. In 1995, after Senator Roth received my letter requesting an independent investigation, Mr. Thorson of the Permanent Subcommittee on Investigations (PSI), was chosen to investigate the 1994 tragic shoot down of two US Blackhawk helicopters. I had written to the PSI after discussions with two people. The first was with a GAO subcommittee investigator who was investigating the DOD response to the Shoot Down for the National Security Committee (previously House Armed Services). And secondly, Ms. Fielder, who contacted me with her account of the professional way the PSI investigation into her son's death by friendly fire from US Army personnel, was handled. Both people left me with the strong feeling that a truly "independent" investigation could only be done by the PSI, because it was an "arms-distance-away" from the DOD and because it had the power to subpoena and take depositions.

On 14 April 1994, in Northern Iraq, two American F15s shot down two US Army Blackhawk helicopters. Twenty-six were killed, fifteen were Americans, and one was our daughter, twenty-five year old Second Lieutenant Laura Piper. The Blackhawk Shoot Down instantly became one of the deadliest friendly fire incidents involving American airplanes in military history. A twenty-one volume military investigation report that concluded the pilots made a reasonable mistake left the families of the victims still seeking the truth. During a court-martial trial of a lower ranking air controller, which resulted in a jury verdict of nullification, the Air Force General who was the pilots' superior officer testified those pilots not only blatantly broke the rules of engagement, but made seven other errors. None of the errors were reasonable. Additionally, the pilot who fired the AMRAAM missile at Laura's helicopter was still flying in the Air Force.

One year had passed and the American families still had questions, no closure, and no accountability. When a family loses a child in the service of this country, it is one of the biggest sacrifices that can be made in the name of freedom and we deserved the truth. It became clear that we needed an independent government investigation. Although the House National Security Subcommittee did hold a hearing in August 1995, only one afternoon was allotted, and it was comprised of mostly read statements. This simply was not enough time to address such a complicated and serious incident.

When we were told, Senator Roth had authorized the PSI to conduct an investigation; we had real hope for the first time. Mr. Eric Thorson led the investigation. Although he was unable to bring the investigation to a final fruition because of the power of the DOD and the realignment of Senator Roth to another committee, it was his efforts that brought

closure to the families and helped heal some of our bitterness. The purpose of government is to serve the needs of its citizens, especially for those families who have made a supreme sacrifice.

In our estimation Mr. Eric Thorson is totally professional, a supreme patriot, and a loyal American who deserves the nomination to the IG of the Small Business Administration. His honesty and integrity are unquestioned. I would be proud to attend your March 1, 2006 Hearing, if permitted.

Sincerely,

Danny Piper, Col (Ret) USAF
1710 Fawn Gate
San Antonio, TX 78248

Joan L. Piper
1710 Fawn Gate
San Antonio, TX 78248
Author of "A Chain of Events"

February 23, 2006

Honorable Olympia Snowe, Chair
Honorable John Kerry, Ranking Minority Member
Committee on Small Business and Entrepreneurship
SR-428A Russell S.O.B.
Washington, D.C. 20510

Dear Senators Snowe and Kerry:

I have been advised that the Committee on Small Business soon will be taking up the nomination of Eric Thorson to be Inspector General of the Small Business Administration. Although Eric is not a close personal friend, I have known him quite well both on and off Capitol Hill for more than 15 years. Accordingly, I am writing to you in strong support of his nomination because I believe that he is an individual of the highest personal integrity and outstanding competence.

I first came to know Mr. Thorson when we both worked for the House Committee On Government Operations (now known as the Committee on Government Reform). I was staff director of that Committee's Subcommittee On Commerce, Consumer and Monetary Affairs for almost 12 years (first under the chairmanship of Congressman Benjamin Rosenthal [D-NY] and then under the chairmanship of Congressman Doug Barnard [D-Ga]). Mr. Thorson was with another subcommittee, the Legislation and National Security Subcommittee.

The principal function of all the subcommittees of Government Operations was Congressional oversight; and, their essential purpose was to ensure the integrity and effectiveness of the operations and programs of federal departments and agencies – a function and purpose very similar to those of the governments' Offices of Inspector General. One of the proudest accomplishments of those of us who served on Government Operations during the 1980s into the early 1990s, was that our investigations and hearings were thorough, non-partisan and conducted in a completely bi-partisan spirit irrespective of which party controlled the Executive Branch. Based on my fairly long association with Eric for a brief period on the Hill and later when we shared a suite of offices in the private sector, I know that these have always been his operating principals.

In considering Mr. Thorson's credentials for the very important IG post, the Committee may be interested in two additional, personal observations: First, the House Subcommittee for which I was staff director had oversight responsibility for the Small Business Administration and examined the working of that agency on a number of occasions. Although the agency certainly has undergone many changes since I left

Capitol Hill, I believe I still retain a good basic understanding of its operations; and I am convinced that the IG post there is a very good match for Mr. Thorson's investigative skills and experience. Second, for several years immediately prior to my leaving the Hill, my subcommittee (which also had investigative jurisdiction for Treasury and IRS) conducted extensive oversight hearings into allegations of serious wrongdoing by certain individuals at the Internal Revenue Service. As a result of those hearings, the Subcommittee concluded that serious abuses had taken place and that the "command and control" structure at the agency was inadequate to prevent the kind of wrongdoing we had investigated. I mention this investigation and its conclusions because I know that Mr. Thorson was involved in a somewhat similar - and I came to learn controversial - investigation of the IRS when he worked for the Senate Finance Committee. Although I had no knowledge of that investigation until I began to read about it in the press, I found it interesting that two entirely separate investigations separated by several years reached quite similar conclusions.

In my personal judgment, if your Committee and the Senate confirm Mr. Thorson, he will become an outstanding, hard working and fair-minded Inspector General.

Finally, I want the Committee to know that although I have provided government relations services to clients for more than a decade, on no occasion have I had any dealings with the Small Business Administration or its programs. Thank you for considering my views.

Respectfully,

Peter S. Barash

February 23, 2006

Honorable John F. Kerry
Ranking Minority
Committee on Small Business and Entrepreneurship
United States Senate
428A Russell Senate Office Building
Washington, DC 20510

Dear Senator Kerry:

This letter is written in strong support for the confirmation of Eric M. Thorson to be the Inspector General of the Small Business Administration.

I have followed Eric's professional career for more than 20 years and I know him to be a highly competent professional with a proven record for protecting the public interest. We first met in the mid 1980's when I served as Chief Counsel and Staff Director for the Subcommittee on Oversight and Investigations under the Chairmanship of the Honorable John D. Dingell.

Testifying before our subcommittee on December 3, 1986, Mr. Thorson described his efforts to insure the Department of the Air Force received the best price for the final purchase of 21 C-5B aircraft. The "Should Cost" panel, under Eric's leadership, was able to achieve savings of almost $300 million for the taxpayer. If our subcommittee budget had allowed, I would have invited him to join our staff.

I watched Eric when he joined the House Government Operations Committee under the chairmanship of the Honorable John Conyers where he continued ferreting out waste, fraud and abuse. His efforts under Senator Roth and the Senate Permanent Subcommittee on Investigations were truly laudatory. In the case of abuses by the Internal Revenue Service, they were, in fact, heroic.

In addition to my professional experiences with Eric, my wife and I and he and his wife have entertained each other in our homes. I have observed his personal conduct and it is above reproach.

In sum, I highly recommend Eric as a proven investigator who will do the Small Business Administration and the American tax payer great credit.

Sincerely,

Michael F. Barrett, Jr.

Responses to
Questions for the Record from Senator John F. Kerry, Ranking Member
Senate Committee on Small Business and Entrepreneurship
Hearing on the Nomination of Eric Thorson for
Inspector General of the Small Business Administration
March 3, 2006

IG Independence:
In January, the IG's office came to the Hill to brief staffs of members of the Senate Committee on Small Business and Entrepreneurship on its audit of the SBA's administration of the 7(a) Supplemental Terrorist Activity Relief (STAR) Loan program (Report Number 6-09). A representative from the office of Congressional and Legislative Affairs attended the briefing. For several reasons, this seems inappropriate. One, as indicated by the title, SBA was the subject of the audit, as with most IG investigations, which creates a conflict of interest. Two, briefings are an opportunity for Committee staff to ask questions, and SBA, particularly its political office, should not be able to observe which offices have asked questions, what those questions are, and what the answers are. Given that the IG's office is supposed to be independent of the SBA, I do not believe it is appropriate for the SBA to be present. I do not even believe that SBA should be notified or consulted on setting up the briefings.

Yes, or no, if you are confirmed, under your direction, would the Inspector General allow SBA's political arm, the Office of Congressional and Legislative Affairs, to attend briefings that the IG's office gives to Congressional staff?

ANSWER: No, unless requested by committee staff.

Changing Witness Testimony:
During your testimony, you cited Mr. John Colaprete as an example of a witness from the Finance Committee hearings on the IRS whose testimony you strongly stand by, in light of the GAO claims that witness testimony was inaccurate. My staff has acquired a copy of an April 27, 1999 deposition of Mr. Colaprete in which he stated that his testimony during the Finance Committee hearings was inaccurate. Mr. Colaprete also stated that you changed his testimony a number of times. This witness testimony was one of the cases in which the GAO investigators stated that they believed facts were left out of testimony to increase the credibility of witnesses.

C How do you respond to reports that you changed witness testimony to exaggerate or embellish?

ANSWER: I did not change the witness testimony to exaggerate or embellish. I did attempt to shorten Mr. Colaprete's oral testimony to facilitate its flow. Mr. Colaprete's credibility was clear. The U.S. District Court for the Eastern District of Virginia clearly found that the allegations surrounding Mr. Colaprete's testimony were substantiated. I was not present at the deposition in question, so I cannot comment on what was said there. I have learned that one of the principal GAO investigators, Mr. Don Fulwider, was

for many years a Special Agent with the Internal Revenue Service. It is not clear to me what his role was with respect to the deposition, or whether his association with the IRS was communicated to any witnesses interviewed by him. That association was not communicated in the GAO report, or in Mr. Fulwider's written statement to the committee.

Other Issues:
You have stated that you were the lead investigator for then-Senate Majority Leader Trent Lott into Enron, WorldCom and other corporate scandals. What specific investigative activities did you conduct into corporate wrongdoing during your tenure with Sen. Lott=s office?

C Did your investigation result in any findings or conclusions? Were any of your findings documented?

ANSWER: I was a Special Assistant to Senator Lott from early 1992 through December 31, 1992. He was not the Senate Majority Leader during this period. I was not the lead investigator for him, and did not hold that title. There are no documented findings/conclusions with regard to Enron or WorldCom.

MARKUP OF THE NOMINATION OF ERIC THORSON TO BE INSPECTOR GENERAL OF THE SMALL BUSINESS ADMINISTRATION

THURSDAY, MARCH 9, 2006

UNITED STATES SENATE,
COMMITTEE ON SMALL BUSINESS AND
ENTREPRENEURSHIP,
Washington, D.C.

The Committee met, pursuant to notice, at 2:13 p.m., in room S–216, The Capitol, the Honorable Olympia J. Snowe (Chair of the Committee) presiding.

Present: Senators Snowe, Bond, Burns, Allen, Coleman, Thune, Isakson, Vitter, Enzi, Cornyn, Kerry, Harkin, Landrieu, Cantwell, and Pryor.

The CLERK. Hello, Senator. You're voting for Eric Thorson to be Inspector General of the SBA.

Senator BURNS. Conrad Burns votes aye.

The CLERK. Hello, Senator Bond. We're voting for Eric Thorson to be Inspector General of the SBA.

Senator BOND. Exactly what I want to do.

The CLERK. Senator, you're voting for Eric Thorson to be Inspector General of the SBA.

Senator CANTWELL. Aye.

Senator VITTER. Aye.

The CLERK. Senator, you're voting——

Senator ISAKSON. Isakson votes aye.

The CLERK. Senator, you're voting for Eric Thorson to be the Inspector General of the SBA.

Senator HARKIN. I assume it's yes. Yes, yes, yes, I'm voting for Eric. Good guy.

The CLERK. Senator, you're voting for Eric Thorson to be the Inspector General of the Small Business Administration.

Senator ENZI. Aye.

The CLERK. Thank yoy very much.

Senator Allen, we're voting for Eric Thorson to be Inspector General,

Senator ALLEN. He's a good Virginian. I want him in there. Aye, big aye.

The CLERK. Hello, Senator Landrieu. We're voting for Eric Thorson for the Inspector General of the SBA.

Senator LANDRIEU. Yes.

The CLERK. Thank you, ma'am.

Senator Pryor, we're voting for Eric Thorson to be the Inspector General of the Small Business Administration.

Senator PRYOR. Aye. That was easy.

The CLERK. We're voting for Eric Thorson to be Inspector General of the SBA.

Senator THUNE. Yes.

The CLERK. We're voting for Eric Thorson to be Inspector General of the SBA.

Senator COLEMAN. Aye for Eric Thorson.

The CLERK. Thank you very much.

Senator KERRY. This is the vote?

The CLERK. For Eric Thorson to be Inspector General.

Senator KERRY. Aye.

The CLERK. And you need to cast Senator Bayh's vote by proxy.

Senator KERRY. Aye by proxy. Any other proxies?

The CLERK. Everyone came and voted who's planning to vote. Thank you sir.

Senator Snowe, we're voting for Eric Thorson to be Inspector General of the Small Business Administration.

Chair SNOWE. Aye.

Senator CORNYN. Are we the last ones to vote? It doesn't look like it's going to change the outcome, but I'll vote aye.

Chair SNOWE. Thank you. Thank you all.

[Whereupon, at 2:29 p.m., the committee was adjourned.]

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