United States General Accounting Office

GAO

High-Risk Series

February 1995

Quick Reference Guide

GAO/HR-95-2

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

Comptroller General
of the United States

February 1995

The President of the Senate
The Speaker of the House of Representatives

In 1990, the General Accounting Office began a special effort to review and report on the federal program areas we considered high risk because they were especially vulnerable to waste, fraud, abuse, and mismanagement. This effort, which has been strongly supported by the Senate Committee on Governmental Affairs and the House Committee on Government Reform and Oversight, brought much needed focus to problems that were costing the government billions of dollars.

In December 1992, we issued a series of reports on the fundamental causes of problems in designated high-risk areas. We are updating the status of our high-risk program in this second series.

This Quick Reference Guide summarizes the status of the 18 areas we have tracked over the past few years. For each area, the Guide outlines the problems, root causes, progress, and outlook for the future; identifies a key GAO contact person; and provides a list of related GAO products. Ten of the 18 high-risk areas are discussed in more detail in separate reports that are also part of this series.

In the accompanying Overview report (GAO/HR-95-1), we discuss the urgent need to continue addressing critical

high-risk problems, covering such areas as Defense Department contract and inventory management, revenue collection operations, major lending programs, and oversight of tens of billions of dollars in civilian contracts. We also discuss progress made in many areas; in particular, progress has been significant enough in five areas for us to remove them from our high-risk program. Further, we introduce newly designated high-risk areas, such as serious and long-standing financial management weaknesses in Defense, growing fraudulent tax filings, and several critical information systems modernization projects that are plagued with problems.

Copies of this report series are being sent to the President and the Republican and Democratic leadership of the Congress, committee chairs and ranking minority members, all other members of the Congress, the Director of the Office of Management and Budget, and the heads of major departments and agencies.

Charles A. Bowsher
Comptroller General
of the United States

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Bank Insurance Fund

The Federal Deposit Insurance Corporation (FDIC) was created in 1933 to provide deposit insurance to protect bank depositors. Through the Bank Insurance Fund, FDIC insures deposits of up to $100,000 in about 11,000 federally insured financial institutions.

In the 1980s, the banking industry took on increased risk in its lending activities in response to a shrinking customer base and competition from other domestic and foreign service vendors. These activities carried greater risk of loss to the institutions and to the insurance fund. The risks were exacerbated by weak internal controls, flawed corporate governance systems, and lax regulatory supervision. Deficiencies in existing accounting rules also contributed to the problem by enabling weak institutions to hide the extent of their problems until their losses had substantially increased. These factors culminated in unprecedented numbers of bank failures and insurance losses in the late 1980s and early 1990s, ultimately depleting the Fund's reserves by year-end 1991.

Since 1991, significantly improved economic factors and congressional actions have successfully resolved the problem.

Favorable interest margins and improved asset quality have caused dramatic improvements in the condition and performance of the banking industry, resulting in substantially lower levels of bank failures and costs to the Fund. Congressional action contributed to a rapid rebuilding of the Fund's reserves, as well as providing the framework for safety and soundness in the banking industry to prevent and provide an early warning of problems, such as flawed corporate governance and internal control weaknesses that contributed significantly to bank failures and the depletion of the Fund.

For example, the Omnibus Budget Reconciliation Act of 1990 provided FDIC flexibility in setting premium rates it charges insured institutions. The FDIC Improvement Act of 1991 (FDICIA) increased FDIC's ability to borrow funds if needed and required FDIC to establish a plan to recapitalize the Fund within 15 years. FDICIA also required management and auditor reporting on the effectiveness of internal controls, independent audit committees, safety and soundness standards, prompt corrective actions to minimize losses to the insurance fund and accounting reforms to ensure reliable financial reports.

The legislative reforms have been largely implemented, and current FDIC estimates show the Fund will be recapitalized before the end of 1995. The progress in rebuilding the Fund is significant and the safeguards to address the root causes of the Fund's depletion are now in place. We are therefore removing the Fund from GAO's high-risk program.

We caution that implementation of FDICIA's reforms will continue to require close attention by the Congress, the Administration, and GAO. Past experience has shown how rapidly the Fund can be depleted. Other factors that will need continuing oversight and monitoring include increases in competition and technological advances, the increasing use of derivative products, narrowing interest margins, and a pending disparity between the premiums paid by institutions insured by the Fund and savings associations insured by the Savings Association Insurance Fund. For these reasons, we will continue to closely monitor the Bank Insurance Fund's progress.

Key Contact

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Related GAO Products

Financial Audit: Federal Deposit Insurance Corporation's 1993 and 1992 Financial Statements (GAO/AIMD-94-135, June 24, 1994)

Financial Derivatives: Actions Needed to Protect the Financial System (GAO/T-GGD-94-170, June 23, 1994; GAO/T-GGD-94-169, June 14, 1994; GAO/T-GGD-94-150, May 19, 1994; GAO/T-GGD-94-151, May 19, 1994; GAO/GGD-94-133, May 18, 1994)

1992 Bank Resolutions: FDIC Chose Methods Determined Least Costly, But Needs to Improve Process (GAO/GGD-94-107, May 10, 1994)

Bank Regulation: Consolidation of the Regulatory Agencies (GAO/T-GGD-94-106, Mar. 4, 1994)

Bank Insurance Fund: Review of Loss Estimation Methodologies (GAO/AIMD-94-48, Dec. 9, 1993)

Interstate Banking: Benefits and Risks of Removing Regulatory Restrictions (GAO/GGD-94-26, Nov. 2, 1993)

Bank and Thrift Regulation: Improvements Needed in Examination Quality and Regulatory Structure (GAO/AFMD-93-15, Feb. 16, 1993; GAO/T-AFMD-93-2, Feb. 16, 1993)

High-Risk Series: Bank Insurance Fund (GAO/HR-93-3, Dec. 1992)

Resolution Trust Corporation

In our December 1992 report, we described risks related to the Resolution Trust Corporation's (RTC) asset disposition practices, contracting activities, information systems, and financial management and accountability.[1] In addition, we warned that the thrift cleanup would not be completed by the time RTC sunsets, and the total cost of the cleanup will depend, in part, on how effectively the Federal Deposit Insurance Corporation (FDIC) applies RTC's investment in both processes and skilled personnel to manage the remaining responsibilities.

Congress, RTC, and FDIC have taken actions that address most of RTC's areas of risk. In March 1993, the Chairman of the Thrift Depositor Protection Oversight Board announced that RTC would implement a number of management reforms. Several of the planned reforms addressed aspects of RTC operations that we had reported as entailing the most risk. In December 1993, the RTC Completion Act required RTC to implement 21 management reforms, several of which were similar to those contained in the March 1993 plan. RTC has initiated actions on all of the reforms and most of them are now fully implemented. RTC also

[1]High Risk Series: Resolution Trust Corporation (GAO/HR-93-4, Dec. 1992).

has made other improvements to its operations. Therefore, we have removed RTC's high-risk designation. However, risks that remain should be addressed as RTC completes its mission and transfers responsibilities to FDIC.

Several of the mandated management reforms address contracting activities. RTC, in addition to undertaking implementation of those reforms, has made improvements in its process for awarding contracts and has increased its contract oversight staffing. RTC also has made many improvements to its information systems over the last 2 years. Its system requirements are now better defined and it has completed all its system development projects. In addition, RTC has modified its systems to improve response times and make them easier to use. RTC and FDIC have established a transition team and initiated a joint planning process to facilitate the transfer of assets, personnel, and operations from RTC to FDIC in a coordinated manner.

RTC also has improved internal accounting controls over its receiverships' transactions, accounting operations, and systems. In particular, RTC has established internal control policies, finalized field accounting

procedures, and established controls over receivership receipts and payments. In addition, RTC has implemented several new systems that contribute to improved accountability and reporting.

In the area of asset disposition, RTC has not undertaken the comprehensive sales method comparison we recommended to improve the selection of sales methods, but it established a process for gathering information that may be useful for evaluating some sales techniques. In addition, RTC has implemented mandated reforms related to its marketing and disposition of assets, that should help RTC obtain maximum revenues.

Despite this progress, RTC needs to address some remaining risks. We are concerned that improvements in RTC's asset disposition practices will not fully compensate for the lack of a valid sales method comparison. The absence of such a comparison could hamper transition team efforts to identify which RTC sales methods FDIC should adopt. Likewise, although RTC has made improvements to its contracting activities, weaknesses continue to be identified in RTC's operating controls over contractors that perform services for its receiverships. RTC needs to continue to improve its operating controls to ensure that

it recovers all that it should from its receiverships. Also, RTC needs to increase emphasis on the closing out of contracts.

The transition of RTC operations and workload to FDIC by January 1996 is also a continuing risk. The task of winding down a large and complex organization with thousands of personnel and billions of dollars in assets, while minimizing the adverse consequences, is a very difficult one. For a successful transition, RTC and FDIC will need to ensure that sufficient controls are in place over the assets that will be sold during the final year of RTC's existence, as well as over the assets that will be transferred to FDIC. It also is important that the transition planners give early attention to the quality of data that FDIC will receive from RTC so that RTC will have sufficient time to prepare for and respond to FDIC's information needs.

Another risk that extends beyond the end of RTC involves the long-term viability of the Savings Association Insurance Fund (SAIF), which insures thrift institutions and will have full responsibility for the cost of resolving thrift failures after RTC's responsibility ends. Currently, SAIF is significantly undercapitalized and its high assessment rates are expected to continue.

While the Federal Deposit Insurance Corporation Improvement Act and the RTC Completion Act strengthened SAIF by providing borrowing authority and other access to funding, SAIF's expected high assessment rates may place the thrift industry at a competitive disadvantage when compared to the anticipated lower assessment rates of the Bank Insurance Fund. These circumstances will require continuing attention by FDIC and the Congress.

Key Contact

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Related GAO Products

Resolution Trust Corporation: Interim Report on the Management Reforms in the RTC Completion Act (GAO/GGD-94-114, June 30, 1994).

Financial Audit: Resolution Trust Corporation's 1993 and 1992 Financial Statements (GAO/AIMD-94-148, June 27, 1994).

Resolution Trust Corporation: Oversight of SAMDA Property Management Contractors Needs Improvement (GAO/GGD-94-5, Nov. 30, 1993).

Resolution Trust Corporation: Status of Management Efforts to Control Costs (GAO/GGD-94-19, Oct. 28, 1993).

Resolution Trust Corporation: Data Limitations Impaired Analysis of Sales Methods (GAO/GGD-93-139, Sept. 27, 1993).

Resolution Trust Corporation: Better Assurance Needed That Contractors Meet Fitness and Integrity Standards (GAO/GGD-93-127, July 26, 1993).

Resolution Trust Corporation: Controls Over Asset Valuations Do Not Ensure Reasonable Estimates (GAO/GGD-93-80, Apr. 8, 1993).

Resolution Trust Corporation: Funding, Organization, and Performance (GAO/T-GGD-93-13, Mar. 18, 1993).

Pension Benefit Guaranty Corporation

The Congress passed the Employee Retirement Income Security Act of 1974 (ERISA) to correct weaknesses in the private pension system. ERISA set minimum funding standards for defined benefit pension plans that were intended to ensure funding would be available to pay all promised benefits and established the Pension Benefit Guaranty Corporation (PBGC) to insure guaranteed benefits in underfunded plans that terminate. To protect against fraud, waste, and mismanagement, ERISA established reporting, disclosure, fiduciary, participation, and vesting requirements, which the Department of Labor and the Internal Revenue Service (IRS) are primarily responsible for enforcing.

In December 1992, we reported that PBGC's weak financial condition threatened the pension insurance program.[1] By 1993, the deficit in PBGC's single-employer program was an estimated $2.9 billion. That same year, ongoing single-employer plans insured by PBGC were underfunded by about $71 billion. This large exposure put PBGC at risk and raised concern that, at some point in the future, PBGC might have to seek financial assistance from the U.S. Treasury to meet its obligations. Moreover, the

[1]High-Risk Series: Pension Benefit Guaranty Corporation (GAO/HR-93-5, Dec. 1992)

cash-based federal budget does not provide the Congress with complete information on PBGC's long-term pension insurance commitments. In 1992, we also reported that management deficiencies hindered PBGC's ability to effectively assess and monitor its financial condition; weaknesses in Labor and IRS enforcement programs hindered detection of ERISA violations; and federal regulation and oversight of pension plans' selection of annuity providers needed to be strengthened.

Since we issued the first high-risk report, several events have occurred that, taken together, have improved the financial outlook for PBGC. First, the General Agreement on Tariffs and Trade (GATT), which became law on December 8, 1994, contains provisions to strengthen minimum funding standards and phase out the cap on variable rate premiums paid by underfunded defined benefit pension plans. We reported that most companies with underfunded pension plans will put more money into their plans. The agency estimates that these provisions will lower the underfunding in plans it insures and reduce the deficit in its single-employer program. Second, PBGC improved its internal controls and procedures, enabling us for the first time to

express an opinion on its fiscal year 1992 balance sheet, and took other steps to improve program administration. In addition, Labor and IRS modified their enforcement strategies and targeting procedures to try to more effectively identify plan abuse and took other steps to improve their enforcement programs. Also, Labor and PBGC began preparing guidance, regulations, and legislation to better regulate and oversee pension plans' selection of annuity providers.

These congressional and agency actions should reduce PBGC's exposure to losses and, correspondingly, the risk to the federal government. Therefore, we are removing PBGC from our high-risk program. However, we will continue to monitor the pension insurance program. Likewise, PBGC should monitor GATT's pension funding provisions to ensure that they reduce plan underfunding and improve its own financial condition. To better reflect its long-term pension insurance commitments, PBGC should work to develop an accrual-based budget. PBGC should also continue strengthening its internal controls and financial information systems so it can meet its future program responsibilities. Labor and IRS should continue strengthening their enforcement programs. Labor should

also work with the Congress to enact legislation to improve the usefulness of independent plan audits. Labor and PBGC should continue developing guidance on fiduciary responsibility associated with purchasing annuities and legislation and regulations requiring that participants receive information on annuity selection and insurance coverage.

Key Contact

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Related GAO Products

Private Pensions: Funding Rule Change Needed to Reduce PBGC's Multibillion Dollar Exposure (GAO/HEHS-95-5, Oct. 5, 1994).

Pension Benefit Guaranty Corporation, Fiscal Year 1993 (GAO/AIMD-94-168ML, Aug. 29, 1994).

Pension Plans: Stronger Labor ERISA Enforcement Should Better Protect Plan Participants (GAO/HEHS-94-157, Aug. 8, 1994).

Underfunded Pension Plans: Stronger Funding Rules Needed to Reduce Federal Government's Growing Exposure (GAO/T-HEHS-94-191, June 15, 1994).

Financial Audit: Pension Benefit Guaranty Corporation's 1993 and 1992 Financial Statements (GAO/AIMD-94-109, May 4, 1994).

Private Pensions: Most Underfunded Plan Sponsors Are Not Making Additional Contributions (GAO/T-HRD-93-16, Apr. 20, 1993).

Assessing PBGC's Short-Run and Long-Run Conditions (GAO/T-HRD-93-1, Feb. 2, 1993).

Pension Plans: Hidden Liabilities Increase Claims Against Government Insurance Program (GAO/HRD-93-7, Dec. 30, 1992).

Management of Overseas Real Property

The State Department, through its Office of Foreign Buildings Operations (FBO), has responsibility for managing about 11,000 leased properties and 3,000 U.S.-owned properties valued at about $12 billion. These properties, at over 260 locations worldwide, include embassies and consulates, office buildings, residential units, and undeveloped land. Since the early 1960s, FBO has experienced serious management problems, which have resulted in deteriorated facilities, cost overruns, oversized and unauthorized housing, poor real estate decisions, and questionable expenditures. The primary cause of this condition has been inadequate property maintenance programs, lax oversight of overseas operations, inadequate information systems, and poor planning.

FBO has taken actions to improve its management of overseas real property, many focusing on maintenance issues which we identified as one of the most serious weaknesses in the real property system. FBO's actions have included assigning maintenance professionals overseas, conducting systematic maintenance surveys, establishing two regional maintenance assistance centers, and implementing a facilities evaluation and assistance program to further support post maintenance

programs. FBO has also made significant progress in addressing other management problems. It has (1) conducted overseas financial audits, (2) expanded its planning staff and determined long-range construction and renovation priorities, (3) implemented an information resource management system and upgraded the real estate management system, and (4) established criteria to prioritize capital construction projects and implemented a system to assess contractor performance.

In view of these actions, we are removing State management of overseas real property from our high-risk list. However, because some problems still exist, we will continue to closely monitor the area. Remaining problems include the failure of some posts to follow FBO guidance on facilities assessments, use of routine maintenance funds, and use of information management systems; the lack of consistent monitoring by FBO's area managers; the retention of unused or excess property; and across-the-board inadequacies in the State Department's financial and information management systems. To address continuing problems, FBO should (1) ensure that posts conduct annual facilities condition surveys and fully use automated property

management systems, (2) expand financial audits and area management assessments to better ensure maintenance funds are properly used, and (3) actively consider the sale or lease of high-value or underutilized properties to off-set appropriations requirements. At the same time, the State Department needs to develop reliable financial and information management systems to improve decision-making on real property management.

Key Contact

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Related GAO Products

Department of State IRM: Strategic Approach Needed to Better Support Agency Mission and Business Needs (GAO/AIMD-95-20, Dec. 22, 1994).

Financial Management: State's Systems Planning Needs to Focus on Correcting Long-standing Problems (GAO/AIMD-94-141, Aug. 12, 1994).

State Department: Widespread Management Weaknesses at Overseas Embassies (GAO/T-NSIAD-93-17, July 13, 1993).

State Department: Survey of Administrative Issues Affecting Embassies (GAO/NSIAD-93-218, July 12, 1993).

High-Risk Series: Management of Overseas Real Property (GAO/HR-93-15, Dec. 1992).

Federal Transit Administration Grant Management

The Federal Transit Administration (FTA) administers a program of financial assistance for the providers of urban and rural public mass transportation (grantees). In fiscal year 1994, FTA provided more than $4.6 billion to grantees for the purpose of improving public transportation. FTA monitors grantees' compliance with federal laws and regulations by performing various oversight and grant management reviews, the most prominent of which is the triennial review.

As we reported in 1992, FTA's past oversight and enforcement practices failed to protect the government from waste and mismanagement.[1] Inadequacies in grantees' financial and other management systems led to noncompliance with federal regulations and the improper use of funds. In addition, FTA seldom used its enforcement powers to compel recipients to fix problems, even when the recipients had long histories of noncompliance.

Over the last two years, FTA has made substantial progress in addressing its grant management weaknesses by making a concerted effort to improve its oversight

[1]High-Risk Series: Federal Transit Administration Grant Management (GAO/HR-93-16, Dec. 1992).

procedures and processes and, more importantly, change the attitudes of its oversight staff and grantees towards safeguarding federal funds. FTA has gone from relying primarily on grantee certifications on compliance to implementing various initiatives and putting systems in place which, over time, will provide a framework that will allow FTA to take a more proactive approach to its grant management, oversight, and enforcement responsibilities.

For example, FTA developed a risk assessment program to identify the inherent risk of each grantee and is using it to develop individual oversight strategies based on the risk assigned. FTA has also increased its use of contractors in performing triennial reviews and recently updated its guidance on how to conduct triennial reviews. FTA has also implemented various training courses for FTA staff, contractors and grantees. In addition, FTA is planning to reorganize its operations to focus more on grantee oversight and will be increasing the size of its regional staff in fiscal year 1995 to better implement oversight activities. More importantly, FTA has recently used its most powerful enforcement tool—withholding

funds—to sanction grantees found to be mismanaging their programs.

FTA has demonstrated its commitment to change by the numerous actions it has taken to improve its oversight of grantees that manage millions of dollars in federal transit funds. FTA officials believe these actions will resolve the concerns that put FTA grant dollars at high risk.

We agree that carrying out the initiatives will continue to reduce the risks associated with FTA's grant management program and are taking FTA off our high-risk list. However, we will continue to monitor FTA's progress because many of these actions have only recently been implemented and their ultimate effectiveness cannot be determined at this time. FTA needs to put a mechanism in place for assessing the effectiveness of these changes. For example, establishing performance measures to evaluate the impact of the new enforcement policy could help FTA determine whether the procedures and time frames for working with grantees to affect compliance and impose sanctions are appropriate and are being applied consistently across all FTA regions. Moreover, improvements in grantee submission of quarterly progress reports and

data contained in the triennial review data base could enhance FTA's ability to work with grantees on noncompliance issues.

Key Contact

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Related GAO Products

Mass Transit Grants: If Properly Implemented, FTA Initiatives Should Improve Oversight (GAO/RCED-93-8, Nov. 19, 1992).

Special Report on Contractor Improprieties at an FTA Region II Grantee (GAO/OSI-92-7, Sept. 10, 1992).

Mass Transit Grants: Risk of Misspent and Ineffectively Used Funds in FTA's Chicago Region (GAO/RCED-92-53, Mar. 4, 1992).

Mass Transit Grants: Noncompliance and Misspent Funds by Two Grantees in UMTA's New York Region (GAO/RCED-92-38, Jan. 23, 1992).

Mass Transit Grants: Improved Management Could Reduce Misuse of Funds in UMTA's Region IX (GAO/RCED-92-7, Nov. 15, 1991).

Mass Transit Grants: Scarce Federal Funds Misused in UMTA's Philadelphia Region (GAO/RCED-91-107, June 13, 1991).

Mass Transit: Significant Federal Investment Is Not Adequately Protected (GAO/T-RCED-91-68, June 12, 1991).

Defense Contract Management

In fiscal year 1993, the Department of Defense (DOD) reported spending about $121 billion contracting for goods and services. In 1992, we reported that defective contract pricing was caused by contractors not providing accurate, complete, and current cost of pricing data, as required by law.[1] Since that report, defective pricing has declined significantly. However, defense contractors' performance in correcting significant cost-estimating system deficiencies, which is key to sustaining a reduced risk of defective pricing, has been mixed.

DOD needs to continue emphasizing the importance of expeditiously correcting deficiencies in contractors' cost-estimating systems. DOD should determine why long-standing deficiencies have not been corrected and establish specific time frames for contracting officers to seek guidance about using more severe remedies that are already available and for involving higher level management in resolving significant deficiencies.

While DOD has addressed some contracting problems, we found that serious DOD

[1]High-Risk Series: Defense Contract Pricing (GAO/HR-93-8, Dec. 1992).

financial control weaknesses have resulted in large and numerous erroneous, and in some cases fraudulent, payments to defense contractors. During a 6-month period in fiscal year 1993, defense contractors returned to the government $751 million, and in fiscal year 1994, they returned $957 million. Most returned funds appear to have been overpayments that were detected by the contractors.

To gain control over these troublesome problems, top-level DOD management must intensify its commitment to resolve contract payment disbursement problems. In the short term, DOD's efforts, including its efforts to research problem disbursement transactions and correct errors, will likely reduce the amount of erroneous and fraudulent payments and disbursements not properly matched to obligations. However, DOD will not adequately resolve its disbursement problems until it (1) corrects weaknesses in control procedures that allow problem disbursements to occur, and (2) improves its contract pay and accounting systems.

Finally, weaknesses in contractor procedures for identifying and excluding unallowable costs from overhead

submissions has resulted in DOD reimbursing contractors for unallowable overhead costs. During fiscal years 1991 through 1993, DOD auditors questioned about $3 billion in contractors' overhead charges.

Defense contractors and the Defense Contract Audit Agency (DCAA) share responsibility for identifying unallowable contract costs. While contractors need to strengthen their controls to ensure that they do not charge unallowable contract costs, DCAA needs to improve its audits of contractors' overhead submissions. DCAA may have difficulty increasing audits given the scope of its workload and recent and planned staff reductions.

Additional information on DOD contract management problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-3).

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Related GAO Products

Financial Management: Status of Defense Efforts to Correct Disbursement Problems (GAO/AIMD-95-7, Oct. 5, 1994).

DOD Procurement: Overpayments and Underpayments at Selected Contractors Show Major Problem (GAO/NSIAD-94-245, Aug. 5, 1994).

Contract Pricing: DOD Management of Contractors With High Risk Cost-Estimating Systems (GAO/NSIAD-94-153, July 19, 1994).

Financial Management: Financial Control and System Weaknesses Continue to Waste DOD Resources and Undermine Operations (GAO/T-AIMD/NSIAD-94-154, Apr. 12, 1994).

Contract Pricing: Reasons for the Decline in Reported Defective Pricing (GAO/NSIAD-94-144BR, Apr. 11, 1994).

DOD Procurement: Millions in Overpayments Returned by DOD Contractors (GAO/NSIAD-94-106, Mar. 14, 1994).

Overhead Costs: Unallowable and Questionable Costs Charged by Government Contractors (GAO/T-NSIAD-94-132, Mar. 3, 1994).

Defense Weapons Systems Acquisition

The Department of Defense (DOD) spends about $80 billion annually researching, developing, and procuring weapon systems. Too often, new weapons acquisitions experience cost overruns, performance shortfalls, and schedule delays. Moreover, requirements for some of these costly weapons, particularly since the collapse of the Soviet Union, may be questionable. Despite past efforts to reform the acquisition system, wasteful practices are adding billions of dollars to defense acquisition costs.

In our initial high-risk report, we noted that the underlying cause of these problems is a prevailing culture dependent on generating and supporting weapons acquisitions.[1] Cultural changes are needed to: (1) control interservice competition and self-interest that leads to the acquisition of unnecessary, overlapping, or duplicative capabilities; (2) discourage overselling of programs and high-risk acquisition strategies; (3) limit incorporation of immature technologies into new weapons; and (4) reduce unnecessary and costly government-unique acquisition requirements and specifications.

[1]High-Risk Series: Defense Weapons Systems Acquisition (GAO/HR-93-7, Dec. 1992).

Top DOD management has demonstrated a strong commitment to acquisition reform initiatives. The Packard Commission's acquisition organization and management recommendations have been largely implemented and are becoming institutionalized. For example, the role and authority of the Under Secretary of Defense for Acquisition and Technology is more firmly established. Also, a Deputy Under Secretary of Defense for Acquisition Reform position has been established to initiate, promote, and support key acquisition reform efforts.

In the Secretary of Defense's February 1994 white paper titled Acquisition Reform—A Mandate for Change, he articulates the need for change and presents a vision and strategy for change. A key element of the strategy is greater reliance on commercial products and processes. Also in 1994, the Secretary of Defense launched an effort to reengineer the systems acquisition review process. This effort is intended to reduce non value-added layers of review and oversight.

In addition to DOD's efforts, the Congress has enacted reforms in the Federal Acquisition Streamlining Act of 1994 and in the Defense Authorization Act for Fiscal Year 1994. The

Federal Acquisition Streamlining Act of 1994, among other things, emphasizes greater reliance on commercial products and processes. The act also: (1) raises the dollar threshold for using more simplified small purchase procedures, (2) seeks to constrain low-rate initial production quantities in defense acquisition programs, and (3) requires a performance-based, incentivized approach to managing acquisition programs.

The Defense Authorization Act for Fiscal Year 1994 established the Commission on Roles and Missions of the Armed Forces. This independent Commission is examining key missions to determine the most cost-effective mix of weapons to accomplish those missions and the services' responsibilities. The Commission is also examining whether DOD's weapons acquisition structure is too complex and duplicative.

Success in achieving acquisition reforms will require overcoming cultural and structural barriers—the procurement bureaucracy will not be dismantled overnight. However, the ingredients for making lasting improvements to the weapons acquisition process—the need, the opportunity, and the

leadership—currently exist. Nevertheless, it is too soon to tell how successful DOD will be in overcoming the barriers to change.

Additional information on DOD weapons systems acquisition problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-4).

Key Contact

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Related GAO Products

Navy Modernization: Alternatives for Achieving a More Affordable Force (GAO/T-NSIAD-94-171, April 26, 1994).

Acquisition Reform: Role of Test and Evaluation in System Acquisition Should Not Be Weakened (GAO/T-NSIAD-94-124, Mar. 10, 1994)

Future Years Defense Program: Optimistic Estimates Lead to Billions in Overprogramming (GAO/NSIAD-94-210, July 29, 1994).

Army Acquisition: Information on the Status and Performance of the Javelin Antitank Weapon (GAO/NSIAD-94-122BR, Mar. 9, 1994).

Tactical Aircraft: F-15 Replacement is Premature as Currently Planned (GAO/NSIAD-94-118, Mar. 25, 1994).

Navy Ships: Seawolf Cost Increases and Schedule Delays (GAO/NSIAD-94-201BR, June 30, 1994).

Missile Development: TSSAM Production Should Not Be Started as Planned (GAO/NSIAD-94-52, Oct. 8, 1993).

Antiarmor Weapons Acquisition: Assessments Needed to Support Continued Need and Long-Term Affordability (GAO/NSIAD-93-49, Mar. 4, 1993).

Defense Inventory Management

The Department of Defense (DOD) uses its inventory of spare and repair parts, clothing, medical supplies, and other support items to support its operating forces. In September 1993, DOD reported that the inventory was valued at $77.5 billion. We estimate that about $36.3 billion of that amount was not needed to be on hand to support DOD's war reserve or current operating requirements.[1]

DOD has wasted billions of dollars on excess supplies, burdened itself with the need to store them, and failed to acquire the tools or expertise needed to manage them effectively. Also, DOD frequently overestimated its supply requirements and purchased too much. DOD's Corporate Information Management initiative is suffering from fundamental weaknesses in DOD's implementation strategy, and the Defense Business Operations Fund is not working as DOD had intended.

The current downsizing environment is posing additional challenges for DOD. In order to ensure that high levels of readiness

[1]The $77.5 billion and the $36.3 billion include inventory that has been revalued to reflect the value of items that need to be repaired and the scrap value of items to be disposed of. We estimate that, if all the inventory were valued at its acquisition cost, the values would be $96.8 billion and $48.4 billion, respectively.

are achieved, DOD must adopt new management approaches that will allow it to sustain these high levels while dealing with resource constraints. At the same time, DOD must address the large amount of unneeded inventory currently stored in its warehouses that will continue to drain resources. This problem will only increase as force reductions continue.

DOD's excessive inventories of unneeded items have resulted largely from a culture that believed it is better to overbuy items than to manage with just the amount of stock needed. This culture has been slow to adopt new management practices, technologies, and logistics systems. DOD has failed to adopt comprehensive inventory management practices that result in storing only those items necessary to support operations. DOD has also failed to provide its personnel with the tools and incentives to manage the inventory properly.

To its credit, DOD has achieved some inventory reductions, initiated some pilot projects, and recognized that it must improve its inventory management. However, DOD has made little overall progress in correcting long-standing management problems that perpetuate

buying and holding too much inventory. For example, DOD stores and maintains billions of dollars of unneeded inventory, requirements continue to be overstated leading to unnecessary procurements, and modern commercial practices are not being implemented as fast as possible.

DOD has had limited success with some commercial inventory practices that have substantially reduced costs while meeting managers' inventory needs. However, DOD needs to be more aggressive in changing its inventory management culture in order to ensure high levels of readiness within existing resource constraints. DOD must take advantage of new management practices, technologies, and logistics systems so that inefficiencies can be eliminated and high levels of readiness maintained.

DOD's top management needs to be much more attentive to the Corporate Information Management project and the Defense Business Operations Fund initiative because they will provide managers with the critical tools needed for managing inventory in the future. DOD must also improve the accuracy of inventory data. Finally, congressional oversight is necessary to maintain DOD's focus on these problems.

Additional information on DOD inventory management problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-5).

Key Contact

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202-512-8412

Related GAO Products

Defense Management: Impediments Jeopardize Logistics Corporate Information Management (GAO/NSIAD-95-28, Oct. 21, 1994).

Commercial Practices: Opportunities Exist to Enhance DOD's Sales of Surplus Aircraft Parts (GAO/NSIAD-94-189, Sept. 23, 1994).

Organizational Culture: Use of Training to Help Change DOD Inventory Management Culture (GAO/NSIAD-94-193, Aug. 30, 1994).

Defense Inventory: Changes in DOD's Inventory, 1989-93 (GAO/NSIAD-94-235, Aug. 17, 1994).

Commercial Practices: DOD Could Reduce Electronics Inventories by Using Private Sector Techniques (GAO/NSIAD-94-110, June 29, 1994).

Defense Business Operations Fund: Improved Pricing Practices and Financial Reports Are Needed to Set Accurate Prices (GAO/AIMD-94-132, June 22, 1994).

Army Inventory: More Effective Review of Proposed Inventory Buys Could Reduce Unneeded Procurement (GAO/NSIAD-94-130, June 2, 1994).

High-Risk Series: Defense Inventory Management (GAO/HR-93-12, Dec. 1992).

Internal Revenue Service Receivables

The Internal Revenue Service's (IRS) management of accounts receivable has been recognized by GAO, the Office of Management and Budget, and IRS management as a high-risk area. IRS' poor performance in resolving tens of billions of dollars in outstanding tax delinquencies has not only lessened the revenues immediately available to support government operations, but could also jeopardize future taxpayer compliance by leaving the impression that IRS is neither fair nor serious about collecting overdue taxes.

Despite many IRS initiatives to "fix" the accounts receivable problem, negligible progress has been made. For example, IRS has not yet developed an accounting system that identifies valid and collectible receivables and those that are not, thereby complicating the job of collection personnel trying to resolve individual accounts. Also, over the period 1990 through 1994, the gross inventory of tax debt, which includes accounts receivable, grew about 80 percent—from $87 billion to $156 billion. During the same period, annual collections of delinquent taxes declined from $25.5 billion to $23.5 billion—a decline of about 8 percent.

These disappointing results are indicative of the (1) pervasiveness of problems throughout IRS' processes that cumulate in the inventory and (2) difficulty in coming to grips with the interrelationship of several underlying causes. These include the lack of accurate and reliable management information for determining the validity and makeup of the inventory of tax debt and evaluating the effectiveness of individual collection activities; IRS' lengthy, antiquated, rigid, and inefficient collection process; difficulty in balancing collection efforts with the need to protect taxpayer rights; and a decentralized organization that blurs responsibility and accountability.

In our view, IRS' primary task is two-fold: collect more delinquent taxes and stem the growth in outstanding debts. The first part of the task requires greater efficiency and productivity in the collection process. The second requires changes in other IRS components to prevent delinquencies and minimize cluttering-up the collection process with invalid and uncollectible accounts.

The lack of accurate and reliable information continues to be IRS' foremost problem and hinders most of its efforts to effectively deal with tax debts. Priority must be given to this

area because so many of IRS' modernization efforts rely heavily on accurate and reliable information. IRS also needs to clearly demonstrate the institutional focus necessary to effectively deal with the underlying causes of the problem—causes that cut across the agency and across lines of managerial authority and responsibility. Equally important is that the strategy address ways to best reengineer IRS' outmoded tax collection processes, which were designed decades ago and have not kept pace with advances in technology or communications.

Additional information on problems with IRS receivables can be found in a separate report issued as part of this series (GAO/HR-95-6).

Key Contact

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Related GAO Products

Financial Audit: Examination of IRS' Fiscal Year 1993 Financial Statements (GAO/AIMD-94-120, June 15, 1994).

Tax Administration: Changes Needed to Cope With Growth in Offer in Compromise Program (GAO/GGD-94-47, Dec. 23, 1993).

Tax Administration: Collecting Delinquent Taxes and Communicating with Taxpayers (GAO/T-GGD-94-50, Nov. 9, 1993).

Tax Administration: IRS Can Do More to Collect Taxes Labelled "Currently Not Collectible" (GAO/GGD-94-2, Oct. 8, 1993).

Tax Administration: New Delinquent Tax Collection Methods for IRS (GAO/GGD-93-67, May 11, 1993).

Financial Audit: IRS Significantly Overstated Its Accounts Receivable Balance (GAO/AFMD-93-42, May 6, 1993).

Tax Administration: Improved Staffing of IRS' Collection Function Would Increase Productivity (GAO/GGD-93-97, May 5, 1993).

High-Risk Series: Internal Revenue Service Receivables (GAO/HR-93-13, Dec. 1992).

Managing the Customs Service

In December 1992, we reported that Customs had major weaknesses in (1) mission planning; (2) financial, information, and human resource management; and (3) its organizational structure.[1] Customs lacked an effective strategic management process capable of guiding its operations and establishing accountability for performance. Its prior 5-Year Plan did not set forth a clear objective for its trade enforcement activities, prioritize its numerous objectives, or adequately articulate a means of fully automating Customs' transaction processing. Further, Customs was experiencing related weaknesses in information management, financial management, human resource management, performance measurement, and organizational structure.

Customs has taken action in each of these areas, such as (1) revising its 1993 5-Year Plan to clarify and set priorities for its trade enforcement objectives; (2) improving controls over the identification and collection of duties, taxes, fees, and penalties; (3) reorganizing its debt collection unit, formalizing its collection procedures, and aggressively pursuing collection of

[1]High-Risk Series: Managing the Customs Service (GAO/HR-93-14, Dec. 1992).

delinquent receivables; and (4) embarking on a reorganization plan to correct institutional problems related to cooperation and coordination among its programmatic units and ensure consistency in policy implementation.

Additional efforts will be needed in Customs' financial and information systems modernization programs. For instance, years of inadequate financial management leadership led to deficient financial management systems that do not facilitate financial reporting and control. Recognizing this, Customs stated that it has recently begun to take steps to adopt practices that private and public organizations have used to manage their information resources.

Our recent financial statement audits disclosed that Customs had improvement efforts underway but had not yet fully resolved many of the financial management problems that we reported in 1992. Also, these audits identified two previously unreported problems that relate to Customs' inability to (1) detect and prevent duplicate or excessive claims for refunds of duties and taxes paid on imported goods that are subsequently exported or destroyed and (2) prevent or detect unauthorized access

and modifications to critical and sensitive data and computer programs.[2]

Customs has a wide assortment of plans and a broad reorganization underway that are intended to correct identified management weaknesses, including the additional high-risk areas. Some of these actions can be implemented relatively quickly, while other improvements will take years. While we believe that Customs' planned improvement efforts are appropriately focused, it is important that Customs' top and mid-level management provide the continuing support needed to ensure that these important actions are properly implemented and that related problems do not recur.

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Related GAO Products

Financial Audits: CFO Implementation at IRS and Customs (GAO/T-AIMD-94-164, July 28, 1994).

[2]Our audits also identified a high-risk area related to Customs' inability to control, manage, and report the results of its seizure efforts, including accountability and stewardship over tons of illegal drugs and millions of dollars in cash and other property seized. This area is elaborated on in a separate report issued as part of this series (GAO/HR-95-7).

Financial Audit: Examination of Customs' Fiscal Year 1993 Financial Statements (GAO/AIMD-94-119, June 15, 1994).

Financial Management: Control Weaknesses Limited Customs' Ability to Ensure That Duties Were Properly Assessed (GAO/AIMD-94-38, Mar. 7, 1994).

Financial Management: Customs Did Not Adequately Account for or Control Its Accounts Receivable (GAO-AIMD-94-5, Nov. 8, 1993).

Financial Management: First Financial Audit of Customs Revealed Serious Problems (GAO/T-AIMD-94-3, Oct. 5, 1993).

Financial Audit: Examination of Customs' Fiscal Year 1992 Financial Statements (GAO/AIMD-93-3, June 30, 1993).

Customs Service: Trade Enforcement Activities Impaired by Management Problems (GAO/GGD-92-123, Sept. 24, 1992).

Asset Forfeiture Programs

In our December 1992 high risk report on the asset forfeiture programs of the Department of Justice and the U.S. Customs Service, we reported that major operational problems relating to the management and disposition of seized and forfeited property had been identified and corrective actions were being initiated.[1] Although some management and systems changes have improved program operations, our recent audits of the Customs Service's fiscal year 1993 and 1992 financial statements revealed serious weaknesses in key internal controls and systems that affected Customs' ability to control, manage, and report the results of its seizure efforts, including accountability and stewardship over property seized. As a result, tons of illegal drugs and millions of dollars in cash and other property have been vulnerable to theft and misappropriation. However, Customs recognizes the need for long-term and systematic improvements, and its Commissioner established a senior management task force to review the seized property program in its entirety. Actions are being taken to address the internal control and systems problems; however, these efforts are in various stages of development.

[1]High-Risk Series: Asset Forfeiture Programs (GAO/HR-93-17, Dec. 1992)

Problems also persist with the Marshals Services' maintenance and disposal of seized and forfeited property, according to recent Department of Justice Office of Inspector General audit reports. These audits show the need for continued emphasis on and vigilance over seized property.

We also reported in December 1992, that Justice and Treasury were pursuing an initiative for consolidating post-seizure management of noncash seized property inventories as required by legislation enacted in 1988.[2] Furthermore, in June 1991, we identified substantial savings that could be realized through merging post-seizure property management functions. Although a small scale pilot project for consolidation was in effect from October 1992 through September 1993, no significant progress has been made toward consolidation. Justice and Treasury should aggressively pursue options for efficiency gains through program consolidation.

Our 1992 report highlighted growing interest in the forfeiture programs' application of the asset forfeiture laws. In 1993, the Supreme Court issued three decisions that more clearly define the appropriate use of asset

[2]The Anti-Drug Abuse Act of 1988, P.L. 100-690 (21 U.S.C. 887).

seizure and forfeiture authority. Also, several bills were proposed in the last Congress to limit the use of forfeiture. The Departments of Justice and Treasury have each taken several actions in an effort to strengthen the integrity of the asset forfeiture programs, including implementing new policy guidance. It is too soon to tell whether these recent actions will provide sufficient safeguards against improper seizures. Ensuring that adequate safeguards are in place, and adhered to, will require considerable forfeiture program management attention and oversight in the future.

Additional information on asset forfeiture programs can be found in a separate report issued as part of this series (GAO/HR-95-7).

Key Contact

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Related GAO Products

Financial Audits: CFO Implementation at IRS and Customs (GAO/T-AIMD-94-164, July 28, 1994).

Restitution, Fines, and Forfeiture: Issues for Further Review and Oversight (GAO/T-GGD-94-178, June 28, 1994).

Financial Audit: Examination of Customs' Fiscal Year 1993 Financial Statements (GAO/AIMD-94-119, June 15, 1994).

Financial Management: Customs' Accountability for Seized Property and Special Operation Advances Was Weak (GAO/AIMD-94-6, Nov. 22, 1993).

Financial Management: First Financial Audits of IRS and Customs Revealed Serious Problems (GAO/T-AIMD-93-3, Aug. 4, 1993).

Financial Audit: Examination of Customs' Fiscal Year 1992 Financial Statements (GAO/AIMD-93-3, June 30, 1993).

Medicare Claims

In fiscal year 1994, federal spending for the Medicare program totaled $162 billion, or over $440 million a day. The Congressional Budget Office estimates that Medicare spending will reach about $380 billion a year by 2003. Though the portion of Medicare spending attributable to waste, fraud, and abuse cannot be quantified precisely, health care experts have estimated that as much as 10 percent of national health spending is lost to such practices.

In 1992, we reported that Medicare was one of several government programs considered highly vulnerable to waste, fraud, abuse, and mismanagement.[1] Problems we noted included inadequate funding of Medicare claims processing contractors' activities to control fraud and abuse, weaknesses in the Health Care Financing Administration's (HCFA) management of Medicare contractors, flawed payment policies, and weak billing controls. Since then, HCFA has made various regulatory and administrative changes aimed at correcting these problems. However, these worthwhile improvements still are not sufficient to protect Medicare against continued losses.

[1] High-Risk Series: Medicare Claims (GAO/HR-93-6, Dec. 1992).

The funding of contractors' activities to control fraud and abuse has not been commensurate with the growing volume of claims. As a result, today Medicare pays more claims with less scrutiny than at any other time in the last 5 years. Between 1989 and 1994, the requirement for contractors to review a portion of claims in process dropped from 20 percent to 5 percent due to reduced funding. Inadequate funding has also stunted the development of new controls to protect Medicare benefit dollars.

In addition, Medicare claims administration is a complicated process, with some 80 contractors sharing responsibility for claims processing, payment, and review. Because HCFA's management of contractors' antifraud and antiabuse activities provides these contractors with broad discretion, the implementation of payment controls is uneven across the Medicare program.

Furthermore, HCFA is aware that flawed payment policies and abusive billing practices plague Medicare, but the exploitation of the program continues. For example, Medicare has been charged rates as high as $600 per hour for speech and occupational therapy, though therapists' salaries range from under $20 to $32 per

hour. The extraordinary markup between the cost and charges for services is the result of certain weaknesses in payment rules permitted by Medicare.

HCFA has acted to correct certain payment and billing control problems and has initiated two broad efforts to deal with fraud and abuse. In 1993, HCFA established a requirement that raised the standards for contractor performance regarding analyses of payment data. In 1994, the agency awarded a contract for developing a national automated claims processing system intended to replace the several systems currently operating. Through these efforts—promising modern data analysis techniques and greater uniformity in claims processing—HCFA expects to reduce Medicare's inappropriate payments.

The nation's medical service delivery system is becoming more complex. Companies as well as independent providers are delivering health care services and billing Medicare. Even some of Medicare's contractors—which are also private insurers—are investing in provider networks. This means that contractors responsible for reviewing the appropriateness of Medicare claims are also,

in principle, billing Medicare through the networks they own.

However, Medicare's traditional controls against fraud and abuse have not kept pace with health care's more complicated financial arrangements. This situation raises concerns about the government's ability to protect Medicare funds in an increasingly entrepreneurial health care environment.

Additional information on Medicare claims problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-8).

Key Contact

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Related GAO Products

Medicare Part B: Regional Variations and Denial Rates for Medical Necessity (GAO/PEMD-95-10, Dec. 19, 1994).

Medicare: Changes to HMO Rate Setting Method Are Needed to Reduce Program Costs (GAO/HEHS-94-119, Sept. 2, 1994).

Medicare: Inadequate Review of Claims Payments Limits Ability to Control Spending (GAO/HEHS-94-42, Apr. 28, 1994).

Medicare: Greater Investment in Claims Review Would Save Millions (GAO/HEHS-94-35, Mar. 2, 1994).

Medicare: New Claims Processing System Benefits and Acquisition Risks (GAO/HEHS/AIMD-94-79, Jan. 25, 1994).

Medicare: Adequate Funding and Better Oversight Needed to Protect Benefit Dollars (GAO/T-HRD-94-59, Nov. 12, 1993).

Psychiatric Fraud And Abuse: Increased Scrutiny of Hospital Stays Is Needed for Federal Health Programs (GAO/HRD-93-92, Sept. 17, 1993).

Farm Loan Programs

The U.S. Department of Agriculture's (USDA) farm loan program provides temporary financial assistance to farmers who are unable to obtain commercial loans at reasonable rates and terms.[1] The program has two principal and often conflicting roles: (1) to provide high-risk borrowers with temporary credit to enable them to stay in farming until they are able to secure commercial credit and (2) to do so in a way that protects the taxpayers' investment.

In the context of this uncertain operating environment, Farmers Home Adminstration (FmHA) field office lending officials have not always implemented loan-making and loan-servicing standards intended to safeguard federal financial interests or prudently managed farm property that the agency has acquired. Also, some loan-making, loan-servicing, and property management policies do not adequately protect the taxpayers' interests. Furthermore, because legislation has not yet established clear priorities for the agency's fundamental role and mission, losses can be expected to continue.

[1]Within USDA, farm loans have been historically administered by the FmHA. In October 1994, the responsibility was transferred to the newly created Consolidated Farm Service Agency. Because of the general familiarity with the agency's earlier name, we refer to FmHA in this report.

FmHA has taken steps to correct some problems with its farm loan programs. For example, field office lending officials have been provided with extensive training in credit and financial analysis to improve the quality of the loans being made. FmHA reviews show that most new direct and guaranteed loans meet its lending standards. Also, field office officials recently improved their compliance with the standards for servicing guaranteed loans.

However, little progress has been made in correcting other basic problems with the farm loan programs. Field officials still do not always follow established procedures for servicing outstanding direct loans. Also, neither USDA nor the Congress has addressed problems involving loan and property management policies. As a result, the agency continues to, for example, make loans to borrowers who either are behind on repaying their current debts or did not repay their previous debts; reduce and forgive the debts of borrowers who do not repay their loans; and sell farm properties at fixed prices to targeted purchasers, which limits returns and increases holding costs.

The Congress clarified one aspect of the farm loan program when, in late 1992, it

required FmHA to establish programs for beginning farmers and target a certain portion of its loan funds to them. The Congress, however, has not yet provided FmHA with clear direction on being a fiscally prudent lender nor on handling those borrowers who have come to rely on the federal farm loan program as a continuous source of credit.

FmHA's farm loan portfolio continues to contain a high level of delinquent debt, even though billions of dollars in unpaid loans have been forgiven. As of September 1994, FmHA's outstanding farm loans totaled about $18 billion. Of that amount, almost 27 percent—about $4.8 billion—was held by borrowers who were behind on their loan payments. This condition exists even though FmHA lost more than $6 billion during fiscal years 1991 through 1994.

In view of the very tight fiscal constraints that the federal government is facing, action is needed to bring farm loan losses under control. As we reported in December 1992, we believe that the Congress needs to recognize that not all financially stressed farms can be saved and that not all farm families can benefit from a government assistance program intended to keep them in

farming.[2] We suggested that the Congress consider, among other things, giving FmHA firm guidance on: (1) the level of loan losses that the Congress is willing to accept; (2) the length of time over which borrowers should be allowed to receive farm loan assistance; and (3) the kind of assistance, if any, that should be made available to unsuccessful borrowers who want to leave farming.

Additional information on the farm loan programs can be found in a separate report issued as part of this series (GAO/HR-95-9).

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Related GAO Products

Farmers Home Administration: The Guaranteed Farm Loan Program Could Be Managed More Effectively (GAO/RCED-95-9, Nov. 16, 1994).

[2]High-Risk Series: Farmers Home Administration's Farm Loan Programs (GAO/HR-93-1, Dec. 1992).

Debt Settlements: FmHA Can Do More to Collect on Loans and Avoid Losses (GAO/RCED-95-11, Oct. 18, 1994).

Farmers Home Administration: Farm Loans to Delinquent Borrowers (GAO/RCED-94-94FS, Feb. 8, 1994).

GAO High-Risk Program (GAO/AIMD-94-72R, Jan. 27, 1994).

Student Financial Aid

While the Guaranteed Student Loan Program (now known as the Federal Family Education Loan Program (FFELP)) has succeeded in providing access to money for postsecondary education, it has been less successful in protecting the taxpayers' financial interest. In our 1992 report, we focused on several underlying problems with FFELP's structure and management: (1) the structure was inordinately complex, (2) lenders and guaranty agencies had little or no incentive to prevent loan defaults and bore little or no financial risk for loan defaults, and (3) Department of Education management failed to establish adequate controls to minimize its losses and to correct several longstanding management weaknesses.[1]

The Congress and Department of Education have made progress in addressing the underlying problems:

- A significant decline in loan defaults—from $3.6 billion in fiscal year 1991 to $2.4 billion in 1994—was realized, in part, from a 1989 Department initiative and subsequent legislative and administrative actions.

[1]High-Risk Series: Guaranteed Student Loans (GAO/HR-93-2, Dec. 1992).

- The Higher Education Amendments of 1992, which reauthorized the student aid programs, provided stronger enforcement tools and other program enhancements. For example, annual (rather than biennial) financial and compliance audits are to be conducted by independent auditors, and procedures were strengthened over schools allowed to participate in FFELP. Also, the deferment of loan repayments was simplified to provide borrowers a better opportunity to avoid defaulting on their loans when repayment was difficult.
- The Omnibus Budget Reconciliation Act of 1993, which enacted the Student Loan Reform Act of 1993, included additional requirements that provided for lenders and guaranty agencies to share more of the risks and financial costs of FFELP. This legislation also provided for the 5-year phase-in of direct student loans.

However, it is premature to fully evaluate most of the actions being taken. The Congress and Department must continue to address the loan default and program and financial management problems. For example, because reliable student loan data were not available, auditors were unable to express an opinion on whether FFELP's financial statements were fairly stated.

We are revising the definition of this high-risk area because many problems with FFELP may affect the Department's new direct loan program as well as other student financial aid programs. To reduce risks, the Department needs to ensure that improvements made to the gatekeeping process,[2] information and financial management systems, and the programs themselves are effectively implemented. It also needs to continue to expeditiously improve the quality of its student loan data, especially through the implementation of its new student loan data system. Further, the Department must closely monitor its implementation of the direct loan program and the transition from FFELP. The Department needs to formalize its planning for phasing in the Federal Direct Student Loan Program, a critical omission considering well documented problems in FFELP.

We recognize that the legislative and administrative changes, as well as Department initiatives, are steps in the right direction, which, if implemented correctly, could improve the integrity of all federal student aid programs. More information on

[2]Generally refers to the Department's procedures for determining which schools can participate—and whether they should continue participating—in federal student aid programs.

student financial aid program problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-10).

Key Contact

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Related GAO Products

Financial Audit: Federal Family Education Loan Program's Financial Statements for Fiscal Years 1993 and 1992 (GAO/AIMD-94-131, June 30, 1994).

Student Loans: Millions Loaned Inappropriately to U.S. Nationals at Foreign Medical Schools (GAO/HEHS-94-28, Jan. 21, 1994).

Student Financial Aid Programs: Pell Grant Program Abuse (GAO/T-OSI-94-8, Oct. 27, 1993).

Direct Student Loans: The Department of Education's Implementation of Direct Lending (GAO/T-HRD-93-26, June 10, 1993).

Financial Audit: Guaranteed Student Loan Program's Internal Controls and Structure Need Improvement (GAO/AFMD-93-20, Mar. 16, 1993).

Department of Education: Long-Standing Management Problems Hamper Reforms (GAO/HRD-93-47, May 28, 1993).

Department of Housing and Urban Development

The Department of Housing and Urban Development (HUD) is one of the nation's largest financial institutions, insuring some $400 billion in loans and guaranteeing more than $400 billion in outstanding securities for single-family and multifamily housing for a large segment of Americans. It also spends about $25 billion each year furthering the social objectives of providing affordable housing, rent subsidies, and other services to low and moderate income persons (including the homeless) and of helping finance local community development activities.

Four long-standing departmentwide deficiencies led to our designation of HUD as a high-risk area. These deficiencies were weak internal controls, an ineffective organizational structure, insufficient mix of staff with the proper skills, and inadequate information and financial management systems.

Internal control weaknesses, such as a lack of necessary data and management processes, were a major factor leading to the incidents of fraud, waste, abuse, and mismanagement that have come to be known as the 1989 HUD scandals. Organizational problems have included

overlapping and ill-defined responsibilities and authorities between HUD headquarters and field organizations and a fundamental lack of management accountability and responsibility. Having an insufficient mix of staff with the proper skills has hampered the effective monitoring and oversight of HUD programs and the timely updating of procedures. Poorly integrated, ineffective, and generally unreliable information and financial management systems have failed to meet program managers' needs and have not provided adequate control over housing and community development programs.

HUD has made a start in correcting these long-standing deficiencies. HUD's top management team has focused much attention and energy on overhauling the way the agency is operated. The agency has formulated an entirely new management approach and philosophy, balancing risks with results; is implementing a substantial field reorganization; and has plans and has initiated actions that begin to address the four fundamental management deficiencies. However, it is much too early to assess the effectiveness of these actions.

Also, HUD's Secretary recently announced a proposal to "reinvent" the agency over the

next 4 years by consolidating its housing assistance and community development programs into three performance-based block grant funds, transforming public housing to make it more competitive, and changing the Federal Housing Administration into an entrepreneurial government-owned corporation. If implemented, this proposal would shift many program design and implementation responsibilities to states and localities and would change HUD's primary role into that of overseer and information clearinghouse.

Because the proposal is still in the conceptual stage and implementation details are not available, it is difficult to predict how the proposal might affect the corrective actions and plans that HUD already has under way. However, no matter what form HUD finally takes, strong internal controls, an effective organizational structure, a sufficient mix of properly skilled staff, and adequate information and financial management systems will remain key ingredients to the proper management and control of risks. The dialogue on how best to "reinvent" HUD presents the agency, the Office of Management and Budget, and the Congress with an excellent opportunity to

work together to eliminate HUD's four fundamental management deficiencies.

Additional information on HUD problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-11).

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Related GAO Products

Housing and Urban Development: Major Management and Budget Issues (GAO/T-RCED-95-86, Jan. 19, 1995, and GAO/T-RCED-95-89, Jan. 24, 1995).

HUD Information Resources: Strategic Focus and Improved Management Controls Needed (GAO/AIMD-94-34, Apr. 14, 1994).

Multifamily Housing: Status of HUD's Multifamily Loan Portfolios (GAO/RCED-94-173FS, Apr. 12, 1994).

Improving Government: Actions Needed to Sustain and Enhance Management Reforms (GAO/T-OGC-94-1, Jan. 27, 1994).

Government National Mortgage Association: Greater Staffing Flexibility Needed to Improve Management (GAO/RCED-93-100, June 30, 1993).

Multifamily Housing: Impediments to Disposition of Properties Owned by the Department of Housing and Urban Development (GAO/T-RCED-93-37, May 12, 1993).

HUD Reforms: Progress Made Since the HUD Scandals but Much Work Remains (GAO/RCED-92-46, Jan. 31, 1992).

Increasing the Department of Housing and Urban Development's Effectiveness Through Improved Management (GAO/RCED-84-9, Vols. I and II, Jan. 10, 1984).

Department of Energy Contract Management

The Department of Energy (DOE) relies extensively on contractors to manage and operate the nation's nuclear weapons complex and network of national laboratories. In fiscal year 1993, DOE obligated about $15 billion dollars in contracts with 35 commercial firms and academic organizations. As discussed in our 1992 high risk report, DOE's contracting practices have failed to protect the government from fraud, waste, and abuse.[1] Problems have resulted from DOE's (1) almost exclusive use of cost-reimbursement contracts, which offer contractors few incentives to manage and operate the Department's facilities in cost-effective ways; (2) use of contracts that allow the contractors excessive latitude; and (3) inadequate oversight of contractors' activities and costs. In addition, DOE did not require its contractors to prepare auditable financial statements, and the net expenditures reports that contractors did prepare were not being audited every 5 years as required.

Responding to numerous audit findings criticizing DOE's contract management, in 1993 the Secretary of Energy established a

[1]High-Risk Series: Department of Energy Contract Management (GAO/HR-93-9, Dec. 1992).

Contract Reform Team to evaluate the Department's contracting practices and make specific proposals for improvement. In its February 1994 report, the Reform Team recommended 48 actions to improve DOE's contracting practices. These actions included using alternatives to cost-reimbursement contracts, increasing competition for contracts, strengthening financial information systems, and improving DOE's management and control of certain costs.

The milestones set for developing and approving specific plans to implement the recommendations ranged from March 31, 1994, to July 1, 1995. Nineteen of the 29 implementation plans with milestones of October 31, 1994, or earlier, were completed by that date. Once completed, the plans are circulated for comment throughout the Department and submitted to DOE's top managers for approval. After approval, the plans must be implemented. While policy changes can be implemented almost immediately, changes in regulations and procedures will take much longer.

Staff from all organization units are participating in the development of the implementation plans, responsible officials

are being held accountable for action, and top DOE management is overseeing the implementation process. This approach has put DOE well on the way to achieving real changes in the way it conducts its business.

The changes proposed in DOE's current reforms are unprecedented in scope and provide a comprehensive plan to correct the root causes of problems resulting from the Department's past contracting practices. However, designing and administering contract reforms, such as performance-based contracts, will require significant training for staff as well as improved information systems. As we have reported in the past, DOE's previous contract reforms encountered many difficulties because field staff were not trained to administer the contract reforms. We have also reported that DOE has not developed systems to provide the information needed to meet mission needs.

The staff training and information system improvements recommended by the Reform Team are not scheduled to take place until most of the other contract reform initiatives have been implemented. Once again, DOE is introducing policies and reforms before the staff are fully trained to do the work and

before the information systems to provide needed data are fully developed. DOE also has plans to include contractor operations in its agencywide financial statement audits; however, we doubt DOE's ability to accomplish such audits in the near future.

We have targeted DOE's management of its information resources as a focus for our future work and plan to work closely with the Department to develop innovative solutions to improve its financial and management information systems. We will also monitor DOE's implementation of its agencywide financial audit strategy.

Key Contact

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NASA Contract Management

The National Aeronautics and Space Administration (NASA) currently spends over $13 billion annually on procurement—about 90 percent of its budget. Most of this spending is done under contracts that assign almost all technical and cost risk to the government and, since the late 1980s, NASA has been working to improve its ability to oversee its contractors' cost, schedule, and technical performance. However, NASA has had continuing difficulty in managing space projects. For example, most major research and development projects since the late 1970s have required funding increases of at least 50 percent and major completed projects during this same period were launched about 4 years behind schedule.

In our 1992 report, we said that NASA's difficulties in ensuring adequate performance by its contractors and in managing research and development projects were linked primarily to three problems: (1) planned funding levels that exceeded likely budgets; (2) ineffective systems and procedures for overseeing contractors' activities; and (3) NASA field centers' failure to comply with contract management requirements.[1]

[1]High-Risk Series: NASA Contract Management (GAO/HR-93-11, Dec. 1992).

NASA has reported closing the gap of up to $20 billion between its 5-year program plan and its likely budgets. However, whether the gap has actually been closed at the program level is uncertain. For example, within its two largest programs—space shuttle and space station—NASA is not finding it easy to make all the necessary adjustments to align the programs' content and pace to their funding targets.

Successfully dealing with its overall affordability problem will enable NASA to derive maximum benefit from other efforts to improve its management of contracts' cost, schedule, and performance. NASA has been progressing well in several areas, for example, restructuring its award fee policy to emphasize cost control, end products, and performance; reducing the value of contract changes for which prices have not been negotiated; and working to improve the timeliness and accuracy of its contractors' cost and property reporting.

NASA's success in realigning its likely budgets on a program-by-program basis is a key requirement for improving contract management. Any substantial remaining gap will only perpetuate the cost and schedule turbulance of the past.

Beyond the overall affordability issue, NASA's contract management problems are largely due to inadequate enforcement of requirements and lax oversight of contractors. Despite having made progress in some areas, considerable work remains to ultimately effect permanent improvements. Over the last 2 years, there have been continuing problems, especially with inadequate management and use of contract audit services, deficiencies in contractors' cost analyses and reports, and various accountability and control problems with contractors' management of government-owned equipment.

Contract and related financial management problems have plagued NASA for many years and they will not be quickly or easily solved. We are encouraged by NASA's efforts to identify and implement needed improvements in both of these areas. Some of the improvement efforts necessarily change how NASA has historically done business and they significantly affect both the agency's contractors and its own personnel. NASA management needs to continue to be proactive in its efforts—correcting problems as they are identified and developing, implementing, and measuring the effectiveness of its own

improvement initiatives. Over time, sustained and focused management attention promises permanent improvement in contractor oversight across the agency.

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NASA Procurement: Proposed Changes to the Jet Propulsion Laboratory Contract (GAO/NSIAD-93-178, July 15, 1993).

Superfund Program Management

In 1980, the Congress created the Environmental Protection Agency's (EPA) Superfund program to clean up inactive or abandoned hazardous waste sites. Since then, thousands of sites have been discovered. Recent estimates indicate that cleaning up hazardous waste sites—many of which are owned by the federal government—could amount to over $300 billion in federal costs and many billions more in private expenditures.

Under the Superfund law, private parties that are responsible for toxic chemical sites must clean up the contamination themselves or reimburse EPA for doing so. When EPA performs the cleanup, it draws on a legislatively established trust fund. Federal agencies generally must use their annual appropriations, not the trust fund, to clean up their facilities.

As we reported in 1992, certain management problems have put the Superfund program at risk.[1] First, because the costs and magnitude of this effort are so large, funding needs to be allocated where it can reduce the most significant threats to human health and the environment. Yet, EPA has not established

[1]High-Risk Series: Superfund Program Management (GAO/HR-93-10, Dec. 1992).

priorities for cleaning up non-federal sites on the basis of their relative risk. Similarly, the government does not have a priority-setting system for allocating funds to clean up federal sites across agency lines. Second, EPA has recovered from responsible parties only a fraction of the moneys it has spent on cleanups. Finally, while EPA relies heavily on contractors to perform much of its cleanup work, it has only begun to address long-standing deficiencies in its management of Superfund contracts.

Some steps have been taken to address these problems. In recent years, EPA has directed more funds to cleanup efforts that address immediate threats, such as removing drums leaking toxic chemicals at sites. In addition, the administration has established a task force to identify ways to prioritize federal facility cleanups across agency lines. To help recover more of its Superfund expenditures, EPA has initiated a process to recoup contractor costs that it has been excluding in its cost recovery efforts. EPA has also taken actions to strengthen its contract management, for example, by reducing its potential liability to pay damage claims brought against contractors that it indemnifies.

These actions, however, are insufficient. We have suggested that EPA make greater use of risk as a criterion in setting cleanup priorities for non-federal sites. Further to increase the recoveries of Superfund costs, we have recommended that EPA broaden the kinds of indirect program costs that EPA seeks to collect from responsible parties. Finally, EPA needs to sustain its commitment to improving its contract management if long-standing deficiencies are to be rectified.

Additional information on Superfund problems and progress can be found in a separate report issued as part of this series (GAO/HR-95-12).

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Related GAO Products

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Superfund: Reauthorization and Risk Prioritization Issues (GAO/T-RCED-94-250, June 24, 1994).

Federal Facilities: Agencies Slow to Define the Scope and Cost of Hazardous Waste Site Cleanups (GAO/RCED-94-73, Apr. 15, 1994).

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