United States General Accounting Office

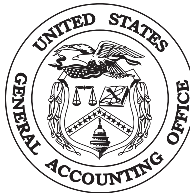
GAO

Performance and Accountability Series

January 2001

Major Management Challenges and Program Risks

Department of the Treasury



GAO-01-254

Contents

Letter 3

Overview 6

Major Performance and Accountability Challenges 13

Related GAO Reports 59

Performance and Accountability Series 63

Comptroller General
of the United States

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

January 2001

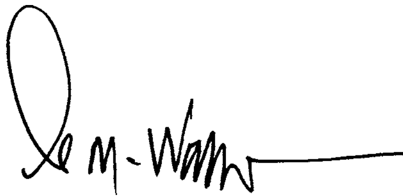
The President of the Senate
The Speaker of the House of Representatives

This report addresses the major performance and accountability challenges facing the Department of the Treasury (Treasury) as it seeks to carry out certain aspects of its economic, financial, enforcement, and management missions. It includes a summary of actions that Treasury has taken and that are under way to address these challenges. It also outlines further actions that GAO believes are needed. This analysis should help the new Congress and administration carry out their responsibilities and improve government for the benefit of the American people.

This report is part of a special series, first issued in January 1999, entitled the Performance and Accountability Series: Major Management Challenges and Program Risks. In that series, GAO advised the Congress that it planned to reassess the methodologies and criteria used to determine which federal government operations and functions should be highlighted and which should be designated as "high risk." GAO completed the assessment, considered comments provided on a publicly available exposure draft, and published its guidance document, *Determining Performance and Accountability Challenges and High Risks* (GAO-01-159SP), in November 2000.

This 2001 *Performance and Accountability Series* contains separate reports on 21 agencies—covering each cabinet department, most major independent agencies, and the U.S. Postal Service. The series also includes a governmentwide perspective on performance

and management challenges across the federal government. As a companion volume to this series, GAO is issuing an update on those government operations and programs that its work identified as “high risk” because of either their greater vulnerabilities to waste, fraud, abuse, and mismanagement or major challenges associated with their economy, efficiency, or effectiveness.



David M. Walker
Comptroller General
of the United States

Overview

The Department of the Treasury is responsible for a broad scope of activities that touch the lives of all Americans, including collecting taxes, managing the government's finances, securing U.S. borders, controlling firearms-related crime, and managing seized assets. To carry out its responsibilities, Treasury has a workforce of about 143,000 employees, most of whom work for Treasury's 13 bureaus. Treasury faces a variety of performance and accountability challenges that affect successful execution of its broad and complex responsibilities. This report discusses the primary challenges that have surfaced on the basis of our work at Treasury and several of its bureaus and describes the progress made since we issued our last performance and accountability report in 1999.[1]

[1] *Performance and Accountability Series: Major Management Challenges and Program Risks: Department of the Treasury* (GAO/OCG-99-14, Jan. 1999).

- Modernize the Internal Revenue Service to better help taxpayers meet their tax responsibilities and to increase overall compliance with tax laws
- Improve the U.S. Customs Service's regulation of commercial trade while ensuring that it protects against the entry of illegal goods at U.S. borders
- Achieve sound financial management through significant management attention and priority
- Improve the Bureau of Alcohol, Tobacco and Firearms' performance measures to better determine its progress in reducing criminals' access to firearms
- Improve the management of Treasury's asset forfeiture program

Internal Revenue Service (IRS) Modernization

IRS' ability to balance its goals of helping taxpayers comply with tax laws and improving overall compliance depends on successfully modernizing IRS. This modernization effort encompasses changes to every facet of IRS' operations, including its organizational structure, its performance management system, and its technology. IRS is about 3 years into the modernization process, which is likely to take a decade or more to complete. Over the past 3 years, IRS has developed and committed to an integrated modernization strategy, which is a significant achievement. It has implemented a new organizational structure with four customer-focused operating divisions to meet the needs of the taxpayer segments they serve. It has also made progress in implementing our recommendations aimed at establishing key management controls needed to

effectively build and implement modern information systems. Substantial work remains for IRS' modernization, however, before expected results are achieved. This work includes

- revamping business practices to better meet taxpayers' needs,
- implementing a balanced approach to performance management to better assess progress in achieving goals and improving operations,
- addressing financial management weaknesses to develop reliable cost-based performance information, and
- institutionalizing effective management controls for information systems modernization.

We have classified four areas of IRS' operations as high-risk: financial management, systems modernization, the collection of unpaid taxes, and noncompliance with the Earned Income Credit (EIC). Two of these areas—financial management and systems modernization—were first designated as high-risk in 1995. In all four areas, billions of dollars are at risk because IRS lacks requisite management controls. Specifically:

- Because IRS lacks reliable cost accounting information, it is difficult for IRS and Congress to determine the cost of various tax collection and enforcement activities. If IRS had such cost accounting information, it could also use it to manage these activities more efficiently.
- Modernization of IRS' systems that support critical IRS business functions has inherent risks because it is extremely complex and costly. In addition, IRS has not yet fully corrected long-standing and serious modernization management and technical weaknesses that were the focus of our past recommendations. If these weaknesses are not fully addressed, modernization projects are at risk of not

performing as intended, costing more, and taking longer to complete.

- IRS lacks reliable and timely financial, operational, and compliance data to help target its effort in collecting billions of dollars in unpaid taxes. As a result, the federal government is exposed to significant losses of tax revenue, and compliant taxpayers bear an undue burden of financing the government's activities.
- IRS lacks data to demonstrate that it has effective controls over noncompliance with the EIC—a tax credit that is available to low-income working people. According to IRS data, taxpayers are inappropriately claiming billions of dollars for this credit.

IRS has made good progress in establishing managerial controls in its financial management and systems modernization areas, but concerted follow-through with modernization plans and substantial implementation is needed to more fully address our recommendations and reduce the risk level.

Customs' Regulation of Commercial Trade

Customs faces significant performance challenges in balancing its responsibilities for enforcing laws to safeguard U.S. borders against the illegal entry of goods and regulating legitimate commercial activity efficiently. Customs has made some progress in implementing modernization initiatives that are designed to improve its regulation of commercial activities and the effectiveness of personal searches of passengers, but the following challenges remain:

- completing an assessment of new trade compliance initiatives as we recommended;
- fully implementing mature and effective system acquisition capabilities as we recommended so that it can effectively acquire a large, complex import processing system known as the Automated

Commercial Environment that is to help facilitate the movement of goods into the United States and the collection of revenues;

- continuing to address our recommendation to obtain better data to improve the process of searching airline passengers who may be carrying contraband, such as illegal drugs, while respecting the rights of American citizens and the traveling public; and
- using reliable data to address our recommendation to determine its staff resource needs for all of its operations and ensure that personnel are located where they are most needed.

Financial Management

Treasury faces many challenges in its ongoing efforts to improve the accuracy and reliability of its financial and information management systems and correct internal control weaknesses that we and the Treasury Office of Inspector General (OIG) identified at several of its bureaus and offices. Treasury received a qualified opinion on its fiscal year 1999 Department-wide financial statements because of financial management problems at IRS and the inability of IRS' administrative systems to produce timely, auditable data to support certain IRS financial statements. Treasury's ability to effectively fulfill its financial management responsibilities has also been adversely affected by the lack of substantial compliance with the financial management systems requirements detailed in the Federal Financial Management Improvement Act of 1996 (FFMIA) and weaknesses in Customs' internal controls over data in its automated systems.

Certain significant financial systems weaknesses; problems with fundamental recordkeeping and financial reporting; incomplete documentation; and weak internal controls, including computer controls, have undermined the U.S. government's ability to obtain an opinion on the reliability of its financial statements for the 3 years that we have reported on these statements. As preparer of

the Financial Report of the United States Government, Treasury's Financial Management Service (FMS) has a key responsibility to provide leadership and work with agencies to address some of these problems, in particular the lack of sufficient systems, controls, and procedures to properly prepare the government's financial statements. Further, in performing much of Treasury's role as primary fiscal agent for the federal government, FMS continues to experience challenges in addressing financial management issues related to implementing the requirements of the Debt Collection Improvement Act of 1996 and improving its computer security controls over systems used to help it process hundreds of billions of dollars of collections and disbursements made on behalf of most federal agencies.

At the end of fiscal year 1998, the unified budget of the federal government was in surplus for the first time in almost 30 years and surpluses are projected to continue over the next decade. As we have stated in previous reports, the transition from annual budget deficits to surpluses presents challenges to Treasury for managing the maturity profile of federal debt held by the public consistent with Treasury's objectives and strategies for achieving these three debt management objectives of sound cash management, lowest financing costs, and the promotion of efficient capital markets.

Bureau of Alcohol, Tobacco and Firearms' Performance Measures

Significant technological advances have given the Bureau of Alcohol, Tobacco and Firearms (ATF) more investigative information to enforce the federal laws and regulations relating to firearms and firearms-related violent crime. However, as we observed in our June 2000 report,[2] it is difficult to determine ATF's progress

[2] *Observations on the Department of the Treasury's Fiscal Year 1999 Performance Report and Fiscal Year 2001 Performance Plan* (GAO/GGD/AIMD-00-231R, June 30, 2000).

because its performance measures are generally output measures (e.g., number of firearm traces made, average trace response time, and number of persons trained), rather than outcome measures (e.g., reductions in firearms-related crimes). Treasury officials have said that until Treasury is better able to determine the cause-and-effect relationships between its programs and the outcomes they are intended to influence, it will continue to rely on output measures.

Asset Forfeiture Program

Another challenge for Treasury deals with the separate but similar seized asset programs operated by Treasury and Justice that were first designated as high risk in 1990. Neither department had adequately focused on managing and accounting for seized assets nor formed a plan to consolidate the two programs, as was mandated by Congress. As of September 30, 1999, the combined value of assets in these two programs was more than $1 billion, of which about $625 million were assets under Treasury's management. We have noted improvements in the management of both programs over the last decade. However, the Treasury Inspector General continues to identify weaknesses in the areas that were the subject of our past recommendations, such as implementing accountability control over seized property at Customs. Further, Treasury and Justice have not addressed our recommendation to consolidate their two programs to eliminate duplication of resources and reduce administrative costs. However, they are conducting a study of opportunities for cooperation in the administration of their programs. We will consider the results of this study along with actions to address internal control weaknesses in determining whether to remove the high-risk designation for the asset forfeiture program in the future.

Major Performance and Accountability Challenges

This report discusses the performance and accountability challenges that have surfaced on the basis of our work at Treasury and several of its bureaus. Those challenges affect Treasury's ability to carry out its critical enforcement and financial responsibilities which include ensuring compliance with tax and trade laws, protecting U.S. borders against the illegal entry of goods, managing the finances of the government, and reducing firearms-related crimes. Although Treasury and its bureaus have made progress in each of these areas, long-standing challenges, some of which rise to the level of high risk, remain. These challenges and high-risk areas are discussed below.

Modernize IRS to Better Help Taxpayers Meet Their Tax Responsibilities and to Increase Overall Compliance With Tax Laws

IRS' ability to balance its goals of helping taxpayers meet their tax responsibilities and improving overall compliance with the tax laws depend on its successful completion of a major modernization effort. This effort is multifaceted and encompasses changes to IRS' organizational structure, business practices, performance management system, and information systems. IRS' organizational restructuring is proceeding reasonably well; however, substantial work remains before expected results are achieved. This work includes

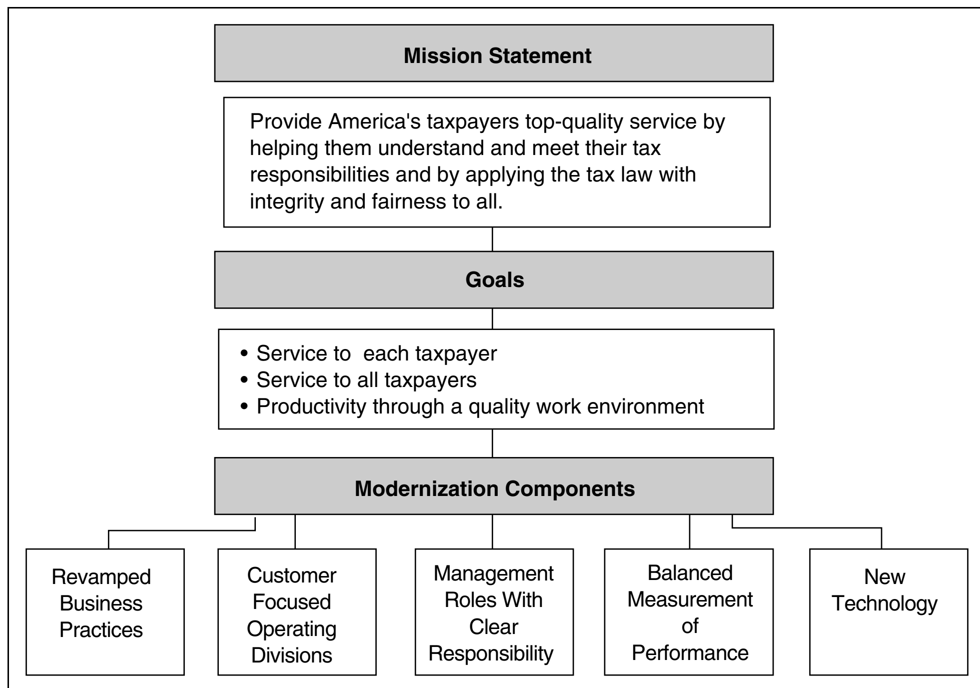
- revamping business practices to better meet taxpayers' needs,
- implementing a balanced approach to performance management to better assess progress in achieving goals and improving operations,
- addressing financial management weaknesses to develop reliable cost-based performance information, and
- institutionalizing effective management controls for information systems modernization.

IRS is now about 3 years into its modernization effort, but improvements in taxpayer service have not yet materialized.[1] Taxpayers continue to be frustrated with IRS' inability to provide telephone customer service. Although the telephone answer rate for the 2000 filing season improved compared to 1999, it was still well below the performance level achieved in 1998. IRS data showed that the answer rate for the 2000 filing season was 62 percent, which is lower than the 72 percent IRS achieved in the 1998 filing season. The answer rate was lower than in 1998 even though IRS, since 1999, has invested heavily in technology to route telephone calls from taxpayers to the location where the wait is shortest and has made telephone assistance available 24 hours a day, 7 days a week. Once taxpayers do get through to IRS, they are often frustrated when employees cannot quickly and accurately answer questions and resolve problems.

Improvements in telephone customer as well as other service improvements should result if IRS is successful at its modernization effort. Figure 1 shows how IRS plans to achieve its mission through five modernization components.

[1] *IRS Modernization: Long-Term Effort Under Way, but Significant Challenges Remain* (GAO/T-GGD/AIMD-00-154, May 3, 2000).

Figure 1: Modernization Promises to Align IRS With Service-oriented Mission and Goals



Source: IRS.

IRS' development of and commitment to an integrated modernization strategy is a significant achievement, but implementation of the modernization strategy may take 10 years or more. Progress thus far has been made in laying a foundation for change. The initial aspects of the modernization effort—the reorganization of IRS' structure, with four customer-focused operating divisions organized around the taxpayer segments they serve—has proceeded reasonably well. The operating divisions are up and running, as of October 2000. Executive leadership teams, which are made up of a combination of career IRS employees and outside hires, have been selected for the divisions; and IRS has been shifting employees to the new organizational structure

in phases. Within each operating division, IRS has identified the key processes—prefiling, filing, and postfiling—that are its primary interactions with taxpayers. Each operating division is to have responsibility for all of the key processes for its respective taxpayer segment.

However, the following key challenges remain.

Revamping Business Practices to Meet Taxpayers' Needs

For the future, IRS must focus on revamping business practices to better meet taxpayer needs. Within the new operating divisions, teams must take a fresh look at how to enforce the tax laws and meet taxpayer needs in new and better ways. This will be a challenge in both overcoming cultural barriers to "thinking outside the box" as well as in coordinating the requisite human capital, data, and information systems support across IRS.

One example of this rethinking is IRS' fresh look at how it provides face-to-face customer service. On the basis of the conclusion that from a taxpayer's perspective, a single point of contact for resolving issues is a good way of doing business, IRS is creating a new position—tax resolution representative. This position is to be staffed with permanent employees at IRS walk-in sites who perform traditional prefiling duties, such as answering tax law questions and helping taxpayers prepare their returns, as well as handling postfiling compliance duties, including installment agreements, account adjustments, and simple audits.

Implementing a Balanced Approach to IRS' Performance Management System to Better Assess Progress

According to our past studies of human capital management, systems for motivating employees and managing their performance must be aligned to support agencies' missions and expectations.[2] At the heart of a performance management system is a set of balanced measures that, if properly used, helps organizations assess progress toward achieving strategic goals and improving operations. IRS has implemented a new balanced measurement system that seeks to develop discrete, corresponding performance measures for each of its three strategic goals—providing top-quality customer service, ensuring taxpayer compliance, and ensuring employee productivity through a quality work environment. Each goal will have measures for customer satisfaction, business results, and employee satisfaction. IRS is aligning its individual performance evaluation systems with its balanced measurement system to clearly link the work of individual managers and employees to the mission and goals of the agency. According to IRS officials, the alignment has been accomplished for managers and executives, and IRS is now in the process of expanding the alignment for its core workforce.

IRS lacks one of its important business-results measures—a measure of taxpayers' voluntary compliance. This measure is a prerequisite to understanding current compliance levels and whether IRS' initiatives will lead to improved compliance. IRS has lacked a voluntary compliance measure for several years and is working to develop one. In the past, IRS used detailed random audits to develop estimates for the level of voluntary compliance, but these audits were the subject of much criticism. In 1995, due to the additional

[2] *Human Capital: A Self-Assessment Checklist for Agency Leaders* (GAO/GGD-99-179, Sept. 1999); and *Human Capital: Key Principles From Nine Private Sector Organizations* (GAO/GGD-00-28, Jan. 31, 2000).

costs and burden that such audits placed on taxpayers, IRS formally cancelled its plans to continue them. We have said that a modified version of the past audits, which reduces burden on taxpayers, could be useful in assessing voluntary compliance. The Commissioner has acknowledged the need for a voluntary compliance measure and has said that in the absence of such a measure, it would be impossible to make informed decisions on the effectiveness of various strategies to encourage voluntary compliance. Accordingly, IRS is working to develop a method for assessing compliance, and we are monitoring IRS' efforts in this regard.

In addition to developing a compliance measure, the next steps for IRS in the area of performance management are to (1) align the balanced measures that it has developed to the employee performance evaluation system, clearly linking the work of individual employees and managers to the mission and goals of the agency; and (2) determine what performance data needs to be collected to track progress. IRS is working on both of these steps.

IRS' human capital problems can be seen as part of a broader pattern of human capital shortcomings that have eroded mission capabilities across the federal government. See our *High-Risk Series: an Update* (GAO-01-263, Jan. 2001) for a discussion of human capital as a newly designated governmentwide high-risk area.

Addressing Financial Management Weaknesses to Develop Reliable Cost-Based Performance Information

Although a balanced measurement system could provide it with information on the results of its programs to improve customer service and increase compliance, IRS also needs to know the cost of achieving these results. Reliable cost information is critical for IRS management and Congress to determine whether IRS has the appropriate levels of funding and staff and is effectively using them. However, serious financial management

weaknesses—a high-risk area since 1995—impair IRS' ability to develop reliable, cost-based performance information.

For example, our audit of IRS' fiscal year 1999 financial statements identified substantial weaknesses in accounting, reporting, and budgetary controls that rendered IRS unable to reliably report how it spent the $8.5 billion that Congress appropriated for it. IRS' lack of cost accounting information has rendered it unable to develop cost-based performance information to measure the effectiveness of its tax collection and enforcement programs and to judge whether it is appropriately allocating available resources among competing management priorities. Consequently, IRS cannot measure the extent to which it is achieving its mission of promoting compliance with federal tax laws. We also found many instances in which expenditures were not promptly charged against related appropriations, and obligations were not deobligated when appropriate.[3] These weaknesses seriously impaired IRS' ability to ensure that resources were spent only in accordance with laws, regulations, and management policy. To address these issues, we have provided IRS with detailed management and operational recommendations. IRS' senior management has been proactive in addressing these issues and has played a major role in the progress IRS has achieved to date. However, resolving many of IRS' most serious problems will require a sustained, long-term commitment of resources, continued involvement of senior management, and sustained progress in systems modernization.

[3]IRS Internal Audit also reported weaknesses in IRS' controls over deobligations in its report entitled *Review of the Need to Deobligate Unliquidated Obligations* (Internal Audit Report No. 084602, June 26, 1998).

Reliable cost-based performance information helps support managerial decisions. IRS has concerns that in view of the congressional and public sensitivity about IRS' collection and enforcement activities, Congress may not be receptive to developing this type of information and including it in the annual budget submission. However, reliable cost-benefit performance information related to these activities is necessary to better assist Congress in making informed funding decisions concerning the appropriate levels and uses of IRS' resources. Consequently, we have recommended that IRS develop this information. We also presented a matter for congressional consideration that Congress should consider requiring IRS to include in any budget request for additional resources for its collection and enforcement activities reliable cost-based performance indicators and other relevant aggregate cost-benefit data that demonstrate the benefits of providing for such resources.[4]

Institutionalizing Effective Systems Modernization Management Controls

The final challenge associated with IRS' modernization effort is institutionalizing effective systems modernization management controls for its information technology (IT) systems—a long-standing challenge that we have designated as a high-risk area since 1995. Over a decade ago, IRS began modernizing its inefficient and outdated systems that are used to process tax returns and respond to taxpayer inquiries. Until IRS' antiquated information systems are replaced, they will continue to hinder efforts to better serve taxpayers through revamped business practices. IRS has made progress over the last several years, particularly since June 2000, in establishing some key management controls. However, to fully address our recommendations and solve the underlying issues, IRS will need to establish all

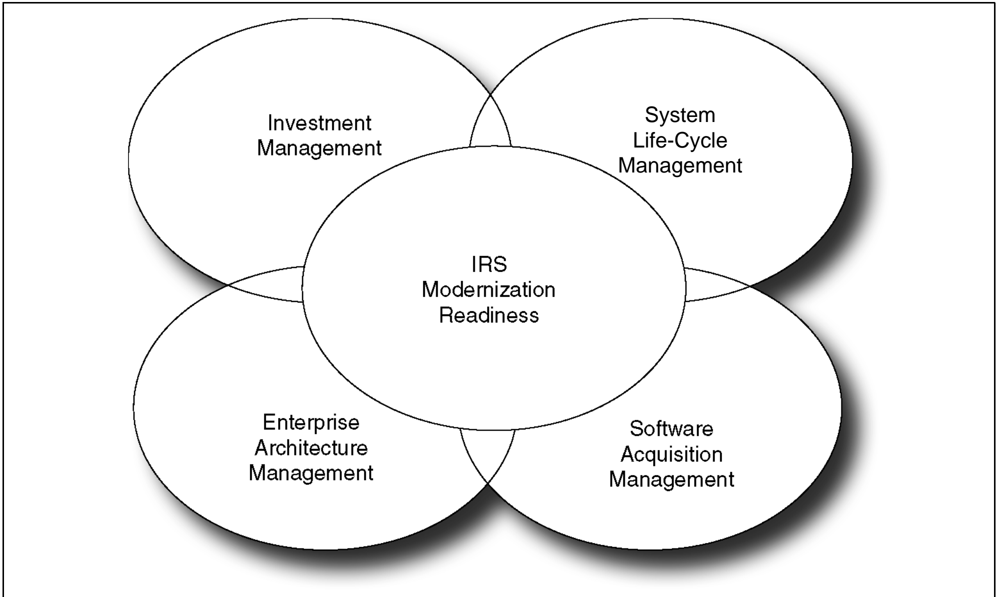
[4] *Internal Revenue Service: Recommendations to Improve Financial and Operational Management* (GAO-01-42, Nov. 17, 2000).

of our recommended controls and ensure that they are implemented. Until this work is completed, IRS' systems modernization will continue to be designated a high-risk area.

Beginning in 1995 and continuing since then, we have made recommendations to correct serious and pervasive management and technical weaknesses, and we concluded that until these weaknesses were corrected, IRS was not ready to invest billions of dollars in building modernized systems.[5] In general, these weaknesses fall into four interrelated and interdependent IT management categories—investment management, system life-cycle management, enterprise architecture management, and software acquisition management (see fig. 2).

[5] *Tax Systems Modernization: Management and Technical Weaknesses Must Be Corrected If Modernization Is to Succeed* (GAO/AIMD-95-156, July 26, 1995).

Figure 2: Categories of IRS' Systems Modernization Weaknesses



Source: GAO analysis of IRS data.

Immediately following our 1995 report, IRS made limited progress in strengthening its modernization management capability. As a result, we suggested in 1996 that the Congress limit IRS' IT spending to certain cost-effective categories. In the fiscal year 1997 Omnibus Consolidated Appropriations Act,[6] Congress directed IRS to develop a plan to correct its weaknesses, including developing and submitting to Congress, by May 1997, an enterprise architecture (or agencywide blueprint for the modernization). In response, IRS took several actions to address congressional direction and implement our recommendations. For example, IRS developed the first two levels of a four-level enterprise

[6] Public Law 104-208.

architecture, which IRS refers to as the Modernization Blueprint.

In September 1997 briefings and a subsequent report in early 1998, we reported that the blueprint was a good first step and made recommendations for completing and implementing it. Subsequently, Congress established a multiyear capital account—the IT Investments Account (ITIA)—to fund IRS systems modernization initiatives and limit IRS' ability to obligate these funds until it met certain conditions.[7] Specifically, IRS was to submit to Congress for approval an expenditure plan that, among other things, (1) implements the blueprint, (2) complies with requirements of the Office of Management and Budget's (OMB) system investment guidelines, (3) passes reviews and approvals by OMB and Treasury's IRS Management Board, and (4) is reviewed by us.

Between May 1999 and October 2000, IRS submitted three expenditure plans and two interim "stop gap" plans, totaling about $477 million, for multiple program and project-level modernization initiatives. This series of plans was consistent with our position that IRS incrementally modernize its systems and submit incremental expenditure plans for release of ITIA funds.[8] Although we found that these expenditure plans generally complied with the legislative conditions and our open recommendations, we also reported that IRS' plans to build systems (i.e., perform detailed design and software development activities) before correcting its long-standing weaknesses introduced a high risk of

[7] See the fiscal year 1998 Treasury and General Government Appropriations Act (P.L. 105-61) and the fiscal year 1999 Omnibus Consolidated and Emergency Supplemental Appropriations Act (P.L. 105-277).

[8] *Tax Systems Modernization: Results of Review of IRS' Initial Expenditure Plan* (GAO/AIMD/GGD-99-206, June 15, 1999).

failure. (Program and project reviews by the Treasury Inspector General for Tax Administration (TIGTA) also found that modernization management controls were lacking.) In response, IRS appropriately restructured its modernization program by scaling back its system development activities and giving priority to putting in place modernization management capabilities and controls.

Since it restructured the program, IRS has made important progress in implementing modernization management capabilities and addressing our recommendations. For example, we reported that IRS had largely defined its system life-cycle methodology that incorporated software acquisition and investment management processes as well as the program roles and responsibilities of IRS and its modernization contractor, and it made progress in producing the first release of its enterprise architecture.

Despite important progress, IRS has more work to do before it will have fully implemented our recommendations and addressed long-standing modernization weaknesses. These efforts include (1) making the program office fully operational, (2) implementing the processes for software acquisition and IT investment management, and (3) completing and implementing its enterprise architecture. IRS has plans and initiatives under way in these areas, but until this work is completed, key modernization management controls are missing, which increases the risk that projects will not perform as intended and will cost more and take longer than they should. As we have consistently stated, these risks are not as severe early in the projects' life cycles, when they are being planned (project definition and design), but they escalate as projects begin to be built (detailed design and software development). Accordingly, we have recommended that IRS refrain from building systems until these controls are in place and functioning.

In addition to institutionalizing effective systems modernization management controls, IRS needs to continue to address the long-standing weaknesses in security controls over its current information systems. Over the past 7 years, we have provided IRS numerous recommendations to assist it in addressing weaknesses in its computer security controls. Major issues addressed by these recommendations include weaknesses in physical security and logical security, data communications management, risk analysis, quality assurance, internal audit and security, security awareness, and contingency planning.

Although IRS has made significant progress in improving computer security weaknesses that we have identified over the last several years, much remains to be done to resolve the serious weaknesses within IRS' computing environment that place its automated systems and taxpayer data at serious risk to both internal and external threats. Despite IRS' extensive reliance on its information systems, IRS continues to have serious weaknesses with general controls designed to protect computing resources, such as networks, computer equipment, software programs, data, and facilities, from unauthorized use, modification, loss, and disclosure. During our audit of IRS' fiscal year 1999 financial statements, we also found that computer security controls over IRS' key applications that manage tax return input and receipt processing do not provide assurance that only authorized personnel have access to the application and related data, that the data are complete and accurate, and that application and data integrity is maintained.

These weaknesses in controls increase the risk that data processed by IRS' information systems are not reliable and continue to expose IRS' tax processing operations to disruption. If IRS does not adequately mitigate these weaknesses, unauthorized individuals could gain access to critical hardware and software, where they may

intentionally or inadvertently add, alter, or delete sensitive data or computer programs. Such individuals could also obtain personal taxpayer information and use it to commit financial crimes in the taxpayer's name, such as fraudulently establishing credit and running up debts.

IRS Faces Challenges in Collecting Unpaid Taxes

Successful modernization should help IRS address aspects of another high-risk area—collection of unpaid taxes. Unpaid taxes include (1) delinquent taxes that IRS is attempting to collect, (2) taxes that IRS knows are due but has decided not to pursue collecting, and (3) an unknown amount of unpaid taxes that IRS has not identified. While IRS has proceeded with its modernization effort, some key collection actions such as levies and seizures have declined since 1997.[9] These declines may increase the incentives for taxpayers to either not report or underreport their tax obligations. Because IRS lacks a measure of voluntary compliance, it does not know the impact of recent declines in collection actions. As a result, we have expanded and renamed the former high-risk area,[10] which encompassed only unpaid taxes known to IRS, to include unpaid taxes that IRS does not know about. As of September 30, 1999, IRS' inventory of known unpaid assessments totaled $231 billion. Of this amount, $127 billion were write-offs that by definition have no future

[9] For example, the number of levies has decreased dramatically from fiscal years 1997 to 2000—from about 3.7 million to about 220,000.

[10] The former high-risk area was called IRS receivables and unpaid tax assessments. Unpaid tax assessments consist of (1) taxes due from taxpayers for which IRS can support the existence of a receivable through taxpayer agreement or a favorable court ruling (federal taxes receivable); (2) compliance assessments in which neither the taxpayer nor the court has affirmed that the amounts are owed; and (3) write-offs, which represent unpaid assessments for which IRS does not expect further collections due to such factors as the taxpayer's death, bankruptcy, or insolvency.

collection potential. The remaining $104 billion has some collection potential and, thus, is at risk.[11]

The former high-risk area was originally designated such in 1990, in part due to serious deficiencies in IRS' information systems. The deficiencies resulted in the lack of sound, reliable information, which hindered IRS' ability to focus collection efforts on those accounts that had the greatest collection potential. These conditions persist. IRS' systems are not integrated; thus, they continue to create high rates of error in taxpayer accounts, which in some cases have led to instances of taxpayer burden and lost revenue to the federal government.

IRS attempts to identify taxpayers who have not paid the taxes they owe through its various enforcement programs. In making decisions about the number and types of enforcement cases to pursue, IRS considers its resources as well as the potential for collection. IRS attributes its inability to fully pursue such cases to a decrease in staff, reassignment of collection employees to support customer service activities, and additional staff time needed to implement certain taxpayer protections that were included in the IRS Reform and Restructuring Act. However, as we previously noted, inadequate financial and operational information has rendered IRS unable to develop cost-based performance information for its tax collection and enforcement programs to judge whether it is appropriately allocating available resources among competing management priorities. These weaknesses continue to expose the federal government to significant losses of tax revenue and increase the burden on compliant taxpayers who

[11] The $104 billion that has collection potential and, thus, is at risk consists of (1) $27 billion in compliance assessments and (2) $77 billion in taxes receivable–$21 billion of which is net taxes receivable and $56 billion of which is an allowance for doubtful accounts.

finance the government's activities. Resolving this high-risk area will require a long-term commitment of resources by IRS and sustained progress in systems modernization.

Noncompliance With EIC

The final IRS high-risk area is noncompliance with EIC.[12] Noncompliance with EIC exposes the federal government to billions of dollars of risk. According to IRS studies, billions of dollars have been overclaimed for this credit. Congress provided IRS with additional funding and enforcement tools to improve EIC compliance. However, IRS does not yet have sufficient data to demonstrate that it has effective controls over EIC noncompliance.

Subsequent to an April 1997 IRS study showing billions of dollars of EIC noncompliance, Congress passed legislation that gave IRS new enforcement tools and additional funding that was specifically designated for EIC-related activities. With those new tools and funds, IRS, in 1998, began implementing a 5-year EIC compliance initiative that involved several components directed at the major sources of EIC noncompliance. For example, IRS initiated enforcement efforts that focused on (1) cases in which an EIC-qualifying child's Social Security number (SSN) was used on more than one tax return for the same tax year and (2) returns filed by certain EIC claimants who used the head-of-household filing status. IRS' efforts have, among other things, reduced the number of EIC-related errors involving SSNs and enabled IRS to stop millions of dollars in erroneous EIC claims.

[12] We have narrowed the focus of the former high-risk area called IRS tax filing fraud that was designated in 1995. It has been renamed "noncompliance with EIC" to better describe the scope of our current concern—billions of dollars for EIC claims that IRS paid but should not have. An unknown portion of erroneous EIC claims is likely attributable to factors other than fraud.

In September 2000, IRS reported the results of a compliance study involving tax year 1997 returns, that is pre-compliance initiative returns.[13] The study showed that of the estimated $30.3 billion in EIC claims made by taxpayers who filed tax year 1997 returns in 1998, an estimated $9.3 billion were invalid (should not have been claimed) and $7.8 billion was actually paid out in improper refunds. These study results generally would not reflect the effect of IRS' 5-year initiative to improve EIC compliance

In July 1998, we recommended that IRS develop evaluation plans for each initiative component to provide timely data for decisionmakers on the interim results of the initiative.[14] IRS is collecting some data on initiative results; however, it is not yet sufficient to determine whether projects have reduced the overall noncompliance rate.

IRS is doing an EIC compliance study of tax year 1999 returns and plans to study tax year 2001 returns. IRS plans to analyze the results of those studies, along with the results of the tax year 1997 study, to measure changes in taxpayer behavior and to determine the effectiveness of the EIC initiative. IRS officials did not know when the results of the tax year 1999 study would be finalized. Until sufficient data are available through these studies or from other sources to demonstrate that IRS has implemented effective controls over EIC noncompliance and the erroneous refunds that result, this will remain a high-risk area.

[13] *Compliance Estimates for Earned Income Tax Credit Claimed on 1997 Returns*, Department of Treasury, Internal Revenue Service, September 2000.

[14] *Earned Income Credit: IRS' Tax Year 1994 Compliance Study and Recent Efforts to Reduce Noncompliance* (GAO/GGD-98-150, July 28, 1998).

Key Contact

James R. White, Director
Tax Issues
(202) 512-9110
whitej@gao.gov

Randolph C. Hite, Director
Information Technology Systems Issues
(202) 512-3870
hiter@gao.gov

Steven J. Sebastian, Acting Director
Financial Management and Assurance
(202) 512-3406
sebastians@gao.gov

Improve Customs' Regulation of Commercial Trade While Ensuring That It Protects Against the Entry of Illegal Goods at U.S. Borders

Customs performs the dual missions of enforcing laws to safeguard U.S. borders against the illegal entry of goods and of regulating legitimate commercial activity. As such, Customs is challenged to balance its security measures with the need to facilitate the flow of cargo and people into the United States. Specifically, the agency's responsibilities include (1) collecting over $20 billion in revenue from imports and enforcing over 400 laws governing international trade, (2) preventing the smuggling of drugs into the country, and (3) overseeing export compliance and money-laundering issues. To carry out these responsibilities, Customs has a workforce totaling almost 20,000 employees at locations around the world.

An overarching challenge for Customs as well as other law enforcement agencies is assessing progress on its key mission areas through outcome-oriented rather than output-oriented performance measures (i.e., succeeding in reducing crime versus making more arrests and convictions). Treasury has said that until it has better data to determine the cause-and-effect relationship between its various programs and the outcomes it is intended to influence, it will continue to use output-oriented performance measures. Accordingly, Customs assesses progress in reducing the flow of illegal drugs by establishing goals for the number of seizures and pounds of illegal substances seized and other output measures. The quantity of narcotics seized in fiscal year 1999 set a record, and Customs met its performance goals for cocaine and marijuana but not for heroin. Customs also reported that its officers processed over 21 million import entries with a value of $977 billion; 137 million conveyances;[15] and 480 million land, sea, and air passengers in fiscal year 1999. However, the degree to which these actions have an impact on safeguarding the borders is uncertain.

In addition to identifying a need for Customs to develop sound output-oriented performance measures, our recent work has identified other performance and management challenges that directly or indirectly affect Customs' efforts to improve security at U.S. borders to safeguard against the illegal entry of goods, including drugs. Although Customs has made some progress in implementing initiatives that are designed to improve the efficiency of its regulation of commercial activities and the effectiveness of personal searches of passengers, the following challenges, all of which have been the subject of our past recommendations, remain: (1) completing an assessment of new trade compliance

[15] Conveyances include aircraft, trucks, trains, buses, privately owned vehicles, and ocean vessels.

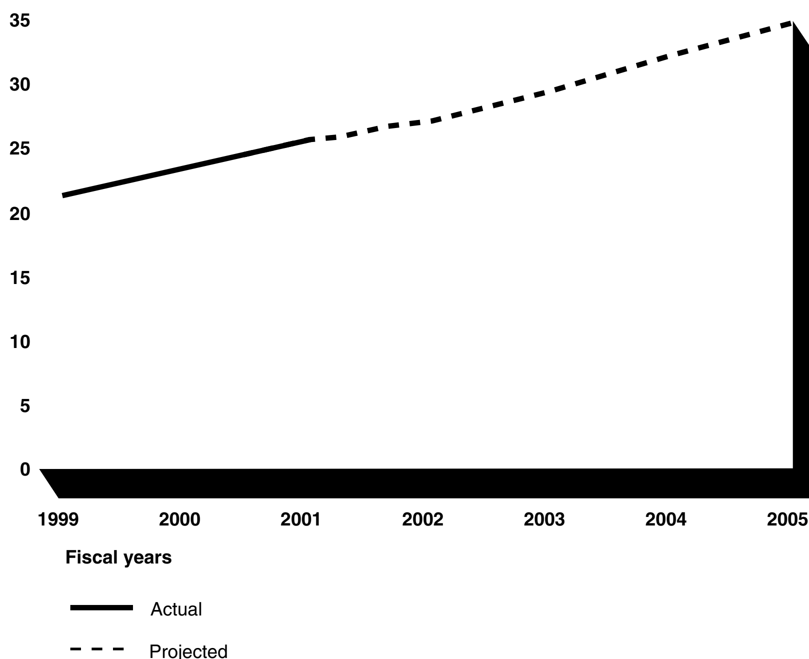
initiatives; (2) acquiring a new import processing system; (3) continuing to improve the process of searching airline passengers who may be carrying contraband, such as illegal drugs, while respecting the rights of American citizens and the traveling public; and (4) using reliable data to determine its staffing needs for all of its operations and ensure that personnel are located where they are most needed.

Impact of New Trade Compliance Initiatives Unclear

Tremendous growth in the world economy creates profound challenges for Customs to facilitate and enforce U.S. trade laws and regulations. The United States is in the midst of a booming era of global trade; and, according to the Commissioner of Customs, the surge in imports and exports will nearly double Customs' workload in the next 5 years alone (see fig.3). To speed the processing of imports and improve compliance with trade laws, Customs has developed a new strategy in response to the Customs Modernization and Informed Compliance Act of 1993 (Mod Act).[16]

[16] Public Law 103-182.

Figure 3: Projected Growth in Entry Summaries for Customs



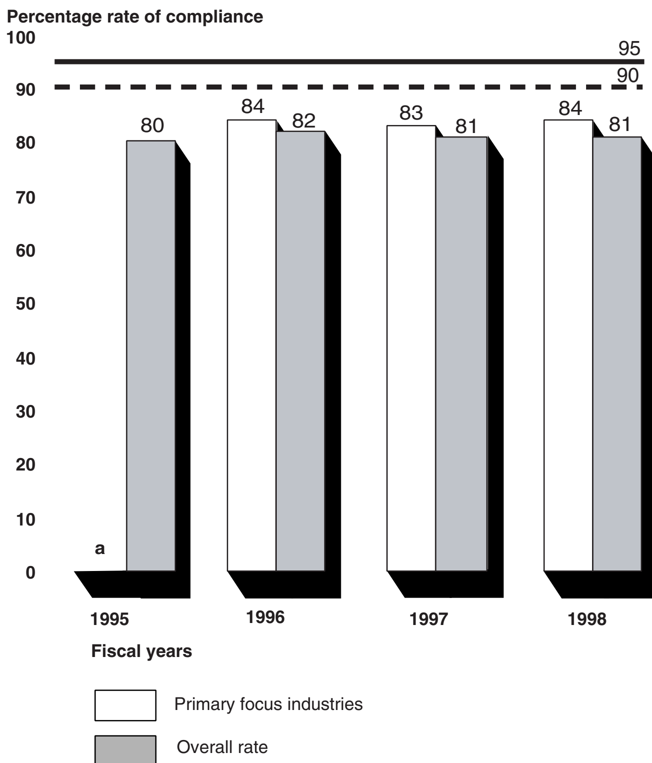
Source: Customs data.

The Mod Act fundamentally altered the relationship between importers and Customs by shifting from Customs to the importer the legal responsibility for declaring the value, classification, and rate of duty applicable to merchandise being imported into the United States. Customs is responsible for determining the final classification and value of the merchandise. The Mod Act also gave Customs and importers a shared responsibility for ensuring compliance with trade laws. To implement these new responsibilities, Customs developed an "informed compliance strategy."

Our review of output statistics indicated that the informed compliance strategy had not yet produced the benefits that were expected.[17] As shown in figure 4, trade compliance rates have remained static at about 81 percent, short of Customs' 90-percent goal. We also found that although Customs had monitored and evaluated certain aspects of the key initiatives and actions, it had not evaluated, nor did it have a plan to evaluate, the impact of the overall informed compliance strategy on compliance with trade laws. Consequently, we recommended that Customs develop and implement an evaluation of the effectiveness of its informed compliance strategy.

[17] *Customs Service Modernization: Impact of New Trade Compliance Strategy Needs to Be Assessed* (GAO/GGD-00-23, Dec. 15, 1999).

Figure 4: Trade Compliance Rates Have Remained Static Between Fiscal Years 1995 and 1999



[a]Customs did not assess compliance rate for PFIs in FY 95.

Note: Entry summaries are required documentation filed with Customs to secure release of imported cargo from Customs.

Source: Customs data.

Customs agreed with our recommendation and stated that it would evaluate the effectiveness of all the initiatives that we assessed, including account management, compliance assessment, compliance measurement, and the informed and enforced compliance programs. Customs said that this extensive study should be completed by February 2001.

Acquisition of New Import Processing System Remains Challenging

Building and deploying a new import processing system is a key component to modernizing how Customs assesses and collects taxes and fees totaling over $20 billion annually at over 300 ports. This large and complex planned system, known as the Automated Commercial Environment (ACE), which is expected to cost over $1 billion, is to replace Customs' antiquated existing system and improve the performance and accountability of Customs' import mission. In short, ACE is to be used to collect, analyze, and disseminate import-related data in a way that will facilitate the trade communities' movement of goods into the United States.

In February 1999, we reported on pervasive management and technical weaknesses facing Customs in building ACE, and we made a series of recommendations that Customs agreed to implement. Specifically, we recommended that before building ACE, Customs (1) have a complete and enforced enterprise architecture; (2) know that ACE was a cost-effective solution and explore alternative system solutions to mission needs, such as another system Treasury was developing known as the International Trade Data System (ITDS); and (3) employ software engineering rigor and discipline.

Customs has taken several important actions to implement our recommendations. For example, Customs has addressed our recommendation for completing and enforcing an enterprise architecture to provide an agencywide business and technological context within which ACE's business value and mission performance can be optimized. Similarly, Treasury and Customs have addressed our concern about possible duplication and incompatibilities between ACE and ITDS by combining the two efforts.

To be successful with ACE, Customs needs to fully implement our recommendations. Customs agrees and

plans additional actions to do so. For example, Customs has committed to seeing that the fundamental acquisition and investment management capabilities that we recommended are in place before investing huge sums of money in ACE. Also, Customs' plans call for investing in ACE incrementally on the basis of a realistic and supportable cost estimate and benefit expectation for each increment. Once an increment is completed, Customs plans to validate that actual costs and benefits are meeting expectations and to use this information in deciding whether to invest in future system increments. Further, Customs still needs to fully implement mature and effective system acquisition capabilities. Because these challenges remain, combined with ACE's mission criticality, we plan to continue monitoring Customs' management of ACE.

Balancing Travelers' Rights With Customs' Responsibility to Interdict Contraband

Congress, in exercising its power to protect the nation's borders, gave Customs broad authority to conduct searches of persons and their luggage. Customs regulations provide that persons, such as passengers coming into the United States, are subject to inspection and search by a Customs officer in order to detect the smuggling of contraband, such as illegal drugs. Concerns have been raised about Customs' policies and procedures for selecting or "targeting" certain passengers for examinations and conducting personal searches, including strip-searches and X-rays.

Inspectors are to select passengers for further examination on the basis of Customs' policies and procedures and their professional judgment and experience. When making a decision to search, inspectors are to consider all the circumstances. Some or mere suspicion is the minimal level required to conduct a patdown search. By policy, Customs requires at least one articulable fact before conducting a patdown search. Supervisory approval is required for any personal search conducted other than a search related to an officer's safety. From our analysis of 102,000 arriving passengers in fiscal years 1997 and 1998 who were subjected to some sort of personal search, we reported that generally, searched passengers of particular races and gender were more likely than other passengers to be subjected to more intrusive types of personal searches (being strip-searched or X-rayed). However, in some cases, the types of passengers who were more likely to be subjected to more intrusive personal searches were not as likely to be found carrying contraband.[18]

We recommended that Customs compare the characteristics of passengers subjected to personal searches with the results of those searches to better target passengers carrying contraband. Customs agreed with our recommendation and said it had already taken steps to develop better data on the results of its searches. By developing improved data and continuing its other management controls, we believe Customs could better safeguard the rights of U.S. citizens and the traveling public while meeting the major challenge of effectively carrying out its drug interdiction mission. During our review of airline passenger targeting, Customs developed additional policies and procedures

[18] *U.S. Customs Service: Better Targeting of Airline Passengers for Personal Searches Could Produce Better Results* (GAO/GGD-00-38, Mar. 17, 2000).

for personal searches that include new requirements for supervisory review and approval and procedures intended to ensure that passengers subjected to personal searches know their rights. We also identified management controls that Customs uses to help ensure that inspectors use their search authority fairly and judiciously. These controls included training for inspectors and supervisors on conducting personal searches and more systematic evaluation of passenger complaints.

Customs reported in October 2000 that reforms initiated to tighten oversight of the searches, such as revising the personal search handbook, have resulted not only in far fewer people being searched but also in the seizure of more contraband. For example, Customs reported that Customs inspectors searched 9,008 airline passengers in fiscal year 2000, a steep reduction from the 23,108 who were searched the previous year. As searches decreased, the seizures of heroin, cocaine, and ecstasy increased from 533 to 665 between fiscal years 1999 and 2000. Overall, drug seizures increased from 1,164 to 1,174 during the same period, according to Customs. The Commissioner of Customs said that the new statistics indicate that Customs is searching fewer innocent travelers while doing a better of job of catching those carrying contraband. The Commissioner acknowledged, however, that the efforts are still in progress and that much more needs to be done.

Using Reliable Data to Determine Staffing Needs

In 1998, we reported on selected aspects of Customs' process for determining its need for inspectors and canine enforcement officers to process commercial cargo or land and sea passengers at all of its 301 ports of entry.[19] We concluded and recommended that for

[19] *Customs Service: Process for Estimating and Allocating Inspectional Personnel* (GAO/GGD-98-107, Apr. 30, 1998).

Customs to successfully implement the Government Performance and Results Act, which requires it to link performance to results, it had to determine its needs for personnel for all of its operations and ensure that personnel are allocated where they are most needed.

In response to our recommendation, Customs awarded a contract for the development of a resource allocation model to estimate the number of inspectors and other personnel needed to process passengers and inspect cargo at all ports of entry. The contractor delivered a prototype to Customs in March 1999.

This was a promising first step, but we continued to monitor the development of the model. In April 2000, we testified that during a review conducted earlier in the year, we found the accuracy and reliability of some input data—such as the estimated time that Customs personnel spent on air and sea passenger processing activities—to be questionable.[20] We concluded that although the model is a potentially viable tool for Customs to use in estimating its personnel needs for now and in the future as imports into the country continue to rise, we believe that more verification needs to be performed on some questionable input data. Customs said that it is still in the early stages of analyzing the model results and fully understanding its capabilities. The original contractor was retained to do additional work to make the model's results more understandable and easier to use. According to Customs officials, the model continues to be reviewed and will be modified as needed to ensure accuracy and validity.

Key Contacts

Laurie E. Ekstrand, Director
Justice Issues

[20] *U.S. Customs Service: Observations on Selected Operations and Program Issues* (GAO/T-GGD/AIMD-00-150, Apr. 20, 2000).

(202) 512-8777
ekstrandl@gao.gov

Randolph C. Hite, Director
Information Technology Systems Issues
(202) 512-6256
hiter@gao.gov

Achieve Sound Financial Management Through Significant Management Attention and Priority

A key to Treasury's ability to effectively carry out its mission both at the Department level and as fiscal agent for the U.S. government is sound financial management, including preparing information about the government's finances that is routinely available, accurate, and reliable. Treasury faces many challenges in its ongoing efforts to improve the accuracy and reliability of its financial and information management systems and correct internal control weaknesses that we and the Treasury OIG identified at several of its bureaus and offices. Without accurate and reliable financial systems and information, as well as sound internal controls, Treasury cannot be sure that the information it has is sufficient to manage day-to-day operations, measure the results of agency and governmentwide operations, account for resources, collect taxes and other debts owed the government, or safeguard assets. Significant top management attention and priority will be required for Treasury to fully address its significant financial management challenges.

Treasury received a qualified opinion on its fiscal year 1999 Department-wide financial statements because of financial management problems at IRS and the inability of IRS' administrative systems to produce timely, auditable data to support certain IRS financial statements. Treasury's ability to effectively fulfill its financial management responsibilities has also been adversely affected by the lack of substantial compliance with the financial management systems requirements

detailed in FFMIA and weaknesses in Customs' internal controls over data in its automated systems.

Certain significant financial systems weaknesses; problems with fundamental recordkeeping and financial reporting; incomplete documentation; and weak internal control, including computer controls, have prevented the U.S. government from obtaining an opinion on the reliability of the government's financial statements for the 3 years that we have reported on these statements. As preparer of the Financial Report, FMS has a key responsibility to work with agencies to address some of these problems, in particular the lack of sufficient systems, controls, and procedures to properly prepare the government's financial statements. Further, in performing much of Treasury's role as primary fiscal agent for the federal government, FMS continues to experience challenges in addressing financial management issues related to implementing the requirements of the Debt Collection Improvement Act (DCIA) of 1996 and improving its computer security controls over systems used to help it process collections and disbursements made on behalf of most federal agencies.

At the end of fiscal year 1998, the unified budget of the federal government was in surplus for the first time in almost 30 years, and surpluses are projected to continue over the next decade. As we have stated in previous reports, the transition from annual budget deficits to surpluses presents challenges to Treasury for managing the maturity profile of federal debt held by the public consistent with Treasury's objectives and strategies for achieving these three debt management objectives of sound cash management, lowest financing costs, and promoting efficient capital markets.

Financial Management Challenges Affecting Certain Bureaus' Operations

For fiscal year 1999, Treasury reported that six of its bureaus' financial management systems did not substantially comply with the requirements of FFMIA. In addition, we reported that IRS continues to experience significant ongoing deficiencies in its financial management and operational systems and processes. Further, Customs also faces financial management problems including weaknesses in its internal controls over data in its automated systems and developing and implementing new automated systems.

Treasury's Financial Management Systems Do Not Substantially Comply With Requirements of FFMIA

FFMIA requires auditors performing financial audits of CFO agencies to report whether agencies' financial management systems substantially comply with federal accounting standards, federal financial management systems requirements, and the Standard General Ledger (SGL) at the transaction level. In fiscal year 1999 and 1998 auditors' reports on compliance with laws and regulations, we and the Treasury OIG identified instances in which Treasury's financial management systems did not substantially comply with the requirements detailed in FFMIA. For fiscal year 1999, Treasury reported that noncompliances were identified at IRS, FMS, Customs, the Departmental Offices, the Office of the Comptroller of the Currency, and the U.S. Secret Service. Generally, the noncompliances involved financial systems that did not allow for the reliable preparation of certain financial statements and reports, lack of or unreliable subsidiary ledgers, general ledgers that did not conform with the SGL, and weaknesses in computer security controls. Under FFMIA, we are required to annually report on agencies' implementation of FFMIA by October 1 of each year. Thus, we will continue to monitor Treasury's efforts to substantially comply with FFMIA.

Financial Management Challenges Continue at IRS

As discussed in an earlier section of this report, IRS continues to experience significant deficiencies in its financial management and operational systems and

processes. Because of these problems, we could not render audit opinions on four of IRS' six financial statements, and our opinion on its balance sheet was qualified for fiscal year 1999. IRS' primary internal control weaknesses relate to its accountability over administrative accounts and budgetary resources, management of taxpayer receipts and data, and management of unpaid tax assessments as well as its computer security controls. To address these issues, we have provided IRS with detailed management and operational recommendations. Although progress has been made to date, resolving many of IRS' most serious problems will require a sustained commitment from senior management.

Customs Continues to Face Financial Management Challenges

Customs continues to face financial management challenges including weaknesses in its internal controls over data in its automated systems, such as systems that are used to account for and manage its collection activity. In addition, as discussed in an earlier section of this report, managerial and technical weaknesses have hindered progress toward developing Customs' planned import system—ACE—which is intended to replace the current system used for collecting import-related data and ensuring, among other things, that trade-related revenue is properly collected and allocated. To ensure proper implementation of important initiatives Customs has planned or under way to address these issues, Customs management must continue to provide the necessary support.

Financial Management Challenges Affecting Treasury's Role as Fiscal Agent

One of Treasury's primary responsibilities is managing the federal government's finances. This massive and complex task includes collecting almost $1.9 trillion in federal tax revenues, making federal payments totaling more than $1.7 trillion, managing federal debt held by the public of about $3.4 trillion, performing central accounting functions, and providing debt management services to federal agencies. Treasury's FMS is the

government's financial manager, central disburser, and collections agency, as well as its accountant and reporter of financial information. Treasury's Bureau of the Public Debt (BPD) is responsible for issuing Treasury securities and accounting for the resulting debt. For the three years that we have audited BPD's Schedules of Federal Debt, we have rendered "clean" opinions on these schedules.

In performing much of Treasury's role as primary fiscal agent for the federal government, FMS faces challenges in addressing financial management issues related to (1) preparing the U.S. government's financial statements, (2) implementing the requirements of the Debt Collection Improvement Act (DCIA) of 1996, and (3) improving the computer security controls used to help it process collections and disbursements made on behalf of most federal agencies. Although FMS has made progress in each of these areas, challenges still remain. It will take a significant and sustained commitment by FMS' management to fully address these challenges. In addition, budget surpluses present challenges to Treasury for managing the federal debt and achieving its debt management objectives.

Preparing Reliable Financial Statements for the Government Continues to Be a Challenge for FMS

In our audit reports on the government's fiscal years 1999, 1998, and 1997 financial statements, we reported certain significant financial systems weaknesses; problems with fundamental recordkeeping and financial reporting; incomplete documentation; and weak internal control, including computer controls. These deficiencies prevented the government from accurately reporting a significant portion of its assets, liabilities, and costs and prevented us from being able to form an opinion on the reliability of the government's financial statements. These deficiencies also affect the reliability of much of the related information in the Fiscal Year 1999 Financial Report and the underlying financial information. In addition, they affect the government's ability to

accurately measure the full cost and financial performance of certain programs and effectively manage related operations. FMS continues to face challenges in working with agencies to address some of these problems, in particular the lack of sufficient systems, controls, and procedures to properly prepare the government's financial statements. Such deficiencies impair the government's ability to (1) properly balance the government's financial statements and account for billions of dollars of transactions between federal government entities, (2) properly and consistently compile the information in the financial statements, and (3) effectively reconcile the results of operations reported in the financial statements with budget results.

We are working with FMS, OMB, and other key agencies to address these deficiencies. However, correcting them is a significant challenge because of the government's size and complexity and the discipline needed to comply with accounting and reporting requirements. Meeting these challenges will require a significant commitment from agencies' and FMS' management, as well as adequately trained staff and effective automated financial and information management systems.

Challenges Remain in Implementing DCIA

As the federal government's central debt collection agency, FMS[21] provides debt management services to federal agencies for nontax debts over 180 days delinquent owed to the federal government. According to Treasury, this debt totaled about $59.2 billion as of September 30, 1999,[22] with Treasury collecting about $2.6 billion during fiscal year 1999, most of which resulted from offsetting tax refunds of delinquent debtors under the Treasury Offset Program (TOP).[23] However, Congress in the past has raised concerns about the slow pace at which Treasury and other agencies have implemented DCIA. According to FMS officials, FMS' debt collection program is not a fully mature program. FMS is actively working to fully implement the provision of DCIA on a phased-in basis over the next few years.

FMS' successful merger of the Tax Refund Offset Program with TOP in 1999 streamlined operations by providing a single point of contact for agencies to refer debts for both tax refund offset and other administrative offset programs. As a result, according to Treasury, offset collections for fiscal year 1999 increased about $570 million over the previous year. According to Treasury officials, system enhancements made during this merger also contributed to increased collections. For example, FMS can now conduct offset matching on both Social Security numbers for joint tax returns, and the system also allows creditor agencies to continuously add and update debt records. Even with these

[21] The Secretary of the Treasury assigned FMS primary responsibility to fulfill Treasury's responsibilities under DCIA.

[22] About $20.7 billion of this amount includes debt that was written off by certain agencies for accounting purposes, but the agencies are still attempting to collect the debts.

[23] In addition to delinquent nontax federal debt, FMS collects child support obligations on behalf of states. During fiscal year 1999, FMS collected about $1.3 billion in child support obligations, representing about half of the collection total.

enhancements, challenges remain for FMS to fully implement TOP. For example, payments for Social Security benefits and more federal salaries still need to be added to TOP. FMS testified in June 2000 that it plans to have such payments available for offset in fiscal year 2001.

In addition to the offset programs, nontax delinquent debt can be transferred to Treasury's centralized collection centers for collection, known as cross-servicing. Cross-servicing may include the use of various debt collection tools, such as private collection agencies (PCAs) and administrative wage garnishment.[24] As we reported in August 2000, FMS collected a relatively small amount of debt through cross-servicing in part because (1) agencies did not always promptly refer eligible debts, and (2) agencies excluded debts from cross-servicing for various reasons, such as debt that is not legally enforceable or debt that Treasury has exempted or waived. At the time of our report, no requirement or process existed for obtaining periodic and independent verification of the accuracy, completeness, and validity of debts agencies reported as eligible or excluded from the DCIA cross-servicing provisions. Moreover, we reported that FMS' staff and some of the PCAs did not always follow established procedures and requirements or effectively use certain debt collection tools. In addition, FMS' method of distributing debts to PCAs—a major debt collection tool—did not fully promote competition, thus limiting the effectiveness of this tool.

Going forward, it will be important for FMS to determine whether its current debt collection strategy and procedures are adequate for optimizing collections

[24] Administrative wage garnishment is a process by which an employee's wages, up to 15 percent of the employee's disposable pay, can be withheld by an employer and paid to the federal government to fulfill an unpaid obligation. FMS officials stated that this tool provides significant opportunities for improved collections of delinquent debts.

through its cross-servicing program and use all available debt collection tools when appropriate, including administrative wage garnishment. Accordingly, we recommended that FMS comprehensively review its cross-servicing process. We also recommended that FMS work with OMB and agencies' Inspector General offices to verify the accuracy and validity of debts agencies report as eligible or excluded from cross-servicing and that it establish and implement procedures for monitoring agencies' written debt referral plans. Further, we recommended that FMS take specific actions to help ensure that a proportionate mix of debts is being distributed to its PCAs and that competition among them is more fully promoted. FMS is currently addressing these recommendations, although it did not agree with all of the specific aspects of our recommendation to comprehensively review its cross-servicing process.

Weaknesses in FMS' Computer Security Controls Continue to Exist

FMS maintains multiple financial and information systems to help it process and reconcile moneys disbursed and collected by the various federal agencies. Our audit for fiscal year 1999 and previous years identified significant computer control weaknesses at each of the FMS data centers. Computer control problems continued to exist at FMS primarily because FMS still lacks an effective, entitywide, computer security management program. FMS' entitywide security control structure has failed to address many of the weaknesses and related significant risks associated with its current and evolving computing environment. The severity of these risks magnifies as FMS expands its networked environment to provide users with greater and easier access to larger amounts of data and system resources. Consequently, billions of dollars of payments and collections are at significant risk of loss or fraud, sensitive data are at risk of inappropriate disclosure, and critical computer-based operations are vulnerable to serious disruptions. We have made numerous recommendations for improvements in FMS' computer

security controls to help reduce the exposure to these risks.

Well-designed and effective computer security controls are essential if FMS' operations and computer resources are to be properly protected. However, it will take a significant and sustained commitment by FMS' management to fully address FMS' computer control weaknesses. FMS officials have recognized the serious nature of these problems and have reported these matters as a material weakness in FMS' Federal Managers' Financial Integrity Act report for fiscal years 1999 and 1998. According to FMS officials, FMS has taken and will continue to take actions to correct the weaknesses we identified and to heighten management focus on security, as well as institute a more systematic and comprehensive computer security management program. We will follow up on these matters during our audit of the federal government's fiscal year 2000 financial statements.

Treasury Faces Debt Management Challenges in a Period of Budget Surpluses

At the end of fiscal year 1998, the unified budget of the federal government was in surplus for the first time in almost 30 years. Budget surpluses continued in fiscal year 1999 and 2000 and are projected to continue over the next decade. Just as budget deficits led to increased borrowing, surpluses over the past three years have resulted in Treasury retiring debt. As we have stated in previous reports, the transition from annual budget deficits to surpluses has consequences for both the profile of federal debt held by the public and Treasury's strategies for achieving its three debt management objectives of sound cash management, lowest financing cost, and promotion of efficient capital markets. Treasury has reduced debt held by the public and managed a declining stock of debt by redeeming maturing debt, reducing the number of auctions and size of new debt issues, eliminating the 3-year note, reopening existing debt issues rather than creating new

issues, conducting “buybacks” of debt before its maturity date, and redeeming callable securities when the opportunity arose. Treasury acknowledges that its future challenges will include making decisions on how to reduce debt while considering such important factors as market adjustments and implications for the Federal Reserve in implementing monetary policy. We are currently conducting a review of how other selected nations have “managed down” their debt and found that these nations have already encountered some of the same challenges and decisions about the debt market facing the United States.

Key Contacts

Gary T. Engel, Director
Financial Management and Assurance
(202) 512-3406
engelg@gao.gov

Paul L. Posner, Managing Director
Strategic Issues
(202) 512-9573
posnerp@gao.gov

Improve ATF’s Performance Measures to Better Determine the Progress in Reducing Criminals’ Access to Firearms

Treasury’s strategic plan includes an objective to deny criminals access to firearms and reduce violent crime, including firearms-related crime. ATF is the Treasury agency responsible for enforcing the federal laws and regulations relating to firearms and reducing firearms-related violent crime. Despite significant technological advances that have given ATF more investigative information to carry out its mission, limitations in its performance measures make it difficult to determine its progress in reducing criminals’ access to firearms and firearms-related crime.

ATF recently reported that in the last decade, technology has brought its investigators and inspectors an enormous increase in investigative information.[25] For example:

- ATF's National Tracing Center has entered in the firearms trafficking information system over 1 million traces of firearms recovered by law enforcement officials.
- The National Integrated Ballistics Information Network, operated by ATF with the Federal Bureau of Investigation (FBI), contains a half-million ballistics images.
- The National Instant Check System, launched by FBI and ATF in 1998, has resulted in ATF receiving over 130,000 reports of prohibited persons attempting to buy firearms from federal firearms licensees.

Regarding progress on denying criminals access to firearms, our June 2000 report[26] on Treasury's fiscal year 1999 performance report and fiscal year 2001 performance plan concluded that it is difficult to determine ATF's progress because ATF's performance measures are generally output measures (i.e., number of firearm traces made, average trace response time, and number of persons trained), rather than outcome measures. Treasury's performance report includes an outcome measure for future crimes avoided, and the data show that Treasury exceeded its goal and increased the number of crimes avoided over 1998. Although this measure does not show reduction in the risk of violent crime, it does estimate the number of crimes prevented through the incarceration of criminals and the

[25] *Following the Gun: Enforcing Federal Laws Against Firearms Traffickers*; Department of the Treasury; ATF (June 30, 2000).

[26] *Observations on the Department of the Treasury's Fiscal Year 1999 Performance Report and Fiscal Year 2001 Performance Plan* (GAO/GGD/AIMD-00-231R, June 30, 2000).

elimination of crime gun sources, according to Treasury's performance report.

In commenting on our June report, Treasury officials stated that the performance measures associated with the challenge of denying criminals access to firearms and reducing firearms-related crime will continue to be output-oriented until Treasury is better able to determine the cause-and-effect relationships between its programs and the outcomes they are intended to influence. They noted that the fiscal year 1999 performance report provides trend data from 1995 through 1998 that is directly related to this outcome—the number of violent crimes committed and crimes committed with firearms. Although having the trend data is helpful, without also having this data for 1999, it is difficult to place ATF's 1999 performance in the appropriate context.

The Treasury OIG has also identified limitations in measuring the impacts of ATF's programs. [27] In its August 2000 report on ATF's Implementation of the youth crime gun interdiction initiative,[28] Treasury's OIG found, among other things, that ATF had not developed

- specific performance measures that show the actual impact on youth violent crime rates in cities as a result of participating in the initiative or

[27] See *Final Report on the Bureau of Alcohol, Tobacco and Firearms' Implementation of the Youth Crime Gun Interdiction Initiative* (Treasury OIG-00-119, Aug. 21, 2000).

[28] The initiative began in 1996 by ATF at the direction of the President to strengthen enforcement efforts against traffickers who supply firearms to youth. Seventeen cities were initially included in the program and were to use ATF's Firearms Tracing System (FTS) to trace every firearm recovered in a crime. ATF was to work jointly with other investigative agencies using FTS trace information to develop investigative and prosecutorial strategies that target traffickers supplying firearms to youth.

- a formal process to verify certain statistics that have been reported to Congress about the program's results.

ATF officials acknowledged that better measures of the initiative's impact are needed and agreed to implement the related recommendation.

Treasury's OIG is currently conducting a review of enforcement performance measures at selected agencies, including those for ATF firearms-related programs, activities, and initiatives, to determine if the measures cover the key aspects of performance in a clear and consistent manner and support departmental goals and objectives.

Key Contact

Laurie E. Ekstrand, Director
Justice Issues
(202) 512-8777
ekstrandl@gao.gov

Improve the Management of Treasury's Asset Forfeiture Program

Treasury and Justice operate similar but separate asset forfeiture programs.[29] As of September 30, 1999, the combined value of assets in these two programs was more than $1 billion, of which about $625 million were assets under Treasury's management. Both programs also hold large amounts of nonvalued assets, such as drugs and weapons. These programs were part of our original high-risk list in 1990 because (1) over the years, neither Treasury nor Justice adequately focused on managing and accounting for seized and forfeited items;

[29] The asset forfeiture program involves the management of property seized in consequence of a violation of public law, including monetary instruments, real property, and tangible personal property of others in the actual or constructive possession of the custodial agency and forfeited property, or property for which the title has passed to the federal government.

and (2) Treasury and Justice had not formed a plan to consolidate postseizure administration of certain properties to eliminate duplication of resources and reduce administrative costs.

We have made several recommendations relating to improving Customs' accountability and stewardship over property seized. Specifically, we have recommended that Customs improve the (1) physical security at its locations used to store seized property, (2) reliability of the information maintained in its seized property tracking systems, and (3) controls over access to critical and sensitive data and computer programs maintained in its systems that account for seized property and law enforcement operations. In recent years, Customs has taken many actions to address our recommendations, such as upgrading existing storage facilities and implementing a new seized property inventory system. These improvements have helped reduce the vulnerability of seized narcotics and other property to theft and misappropriation. In addition, Treasury and Justice are undertaking a joint study to examine the opportunities for increased cooperation in the management of the two programs. However, challenges remain to address the programs' inadequate information systems and financial management weaknesses, including accountability over seized assets. In addition, the results of the joint study are yet to be determined.

Weaknesses Still Exist in Treasury's Asset Forfeiture Program

As we reported in January 1999, a major management challenge facing Treasury's asset forfeiture program is the need to address weaknesses in the department's accountability for and reporting of seized and forfeited property. The Treasury OIG fiscal year 1999 audit findings also suggest that accountability control over seized property needs improvement. Further, Treasury reported instances of material nonconformance with provisions of FFMIA involving Customs' Seized Asset

and Case Tracking System (SEACATS) and the Secret Service's Seized Property Systems in its fiscal year 1999 Accountability Report.

In January 1999, we reported that Customs had made significant systems enhancements and was in the process of further enhancing the security over seized assets and the reliability of information maintained in SEACATS. According to Customs' Fiscal Year 1999 Accountability Report, additional functionality to enhance reporting functions for property and currency was added to SEACATS. However, in January 2000, Treasury's OIG reported that the SEACATS data could not be relied on for financial reporting purposes without substantial manual reconciliation. Consequently, SEACATS could not produce the analysis of changes in seized currency for Customs' seized and forfeited property financial statement disclosure. The OIG listed several recommendations to resolve this issue and other weaknesses in Customs' core financial systems, including developing a comprehensive plan to identify the general ledger system modifications needed to capture financial transactions as they occur.

In its audit of Customs' fiscal year 1999 financial statements, Treasury's OIG also found that accountability controls over the inventory of seized property needed improvement. Specifically, the OIG reported that nine narcotic items could not be located or accounted for during a Customs seized property inventory conducted in September 1999. Furthermore, six of these nine items had been identified as missing during the previous fiscal year inventory, and Customs had not made the required notification to Internal Affairs. The OIG recommended that Customs (1) determine why the six seizures identified as missing during the fiscal year 1998 annual physical inventory verification were not reported to Internal Affairs and (2) complete the current investigation expeditiously and take appropriate action as a result of its findings.

According to Treasury's fiscal year 1999 accountability report, Treasury plans several short- and long-term actions to correct identified weaknesses in the automated systems used to track and report on seized and forfeited assets. Because Treasury believes that its annual assurance and compliance reporting for the Federal Managers' Financial Integrity Act and FFMIA is the proper forum for providing corrective actions, Treasury's fiscal year 2001 performance plan and Customs' fiscal year 2001 performance plan did not include goals or measures of progress related to the asset forfeiture program's management challenges. However, as we reported in June 2000, it would be useful for Treasury to include measures showing its progress toward correcting its material weaknesses in its annual performance plan. Treasury reported that it is working closely with its bureaus, including Customs and the Secret Service, on developing and executing all remediation plans to correct weaknesses identified in its asset forfeiture program. Such support and oversight should help overcome the deficiencies in this program. We will continue to monitor progress in addressing these issues.

Seized Asset Management Programs Not Yet Consolidated, but Under Study

Legislation in 1988 required Treasury and Justice to develop a plan to consolidate their seized property management functions. In 1991 we recommended they consolidate the postseizure management and disposition of noncash seized properties to reduce administrative costs. Although the Departments have not made plans for consolidating their programs, in September 2000, they contracted for a study to identify opportunities for increased cooperation and sharing of agency and contractor resources. The study is to result in recommendations for improving the effectiveness and efficiency of property management functions within the federal asset forfeiture program. Although the study is not expected to fully embrace the concept of consolidating the two separate, seized asset

management and disposal functions, we believe that taking advantage of opportunities for cooperation and sharing of agency and contractor resources encompasses the spirit of the recommendation designed to reduce the programs' administrative costs.

To determine whether to remove the asset forfeiture programs from the high-risk list, we will consider the results of Treasury's and Justice's study, including the implementation of any related recommendations, as well as the results of ongoing initiatives for resolving Treasury's and Justice's respective management and accountability issues.

Contacts

Gary T. Engel, Director
Financial Management and Assurance
(202) 512-3406
engelg@gao.gov

Richard M. Stana, Director
Justice Issues
(202) 512-8777
stanar@gao.gov

Related GAO Reports

IRS Modernization

Tax Administration: Assessment of IRS' 2000 Tax Filing Season (GAO-01-158, Dec. 22, 2000).

Internal Revenue Service: Recommendations to Improve Financial and Operational Management (GAO-01-42, Nov. 17, 2000).

Tax Systems Modernization: Results of Review of IRS' August 2000 Interim Spending Plan (GAO-01-91, Nov. 8, 2000).

Customer Service: Human Capital Management at Selected Public and Private Call Centers (GAO/GGD-00-161, Aug. 22, 2000).

Tax Administration: IRS Faces Several Challenges as It Attempts to Better Serve Small Businesses (GAO/GGD-00-166, Aug. 10, 2000).

Tax Systems Modernization: Results of Review of IRS' March 7, 2000, Expenditure Plan (GAO/AIMD-00-175, May 24, 2000).

IRS Modernization: Long-term Effort Under Way, but Significant Challenges Remain (GAO/T-GGD/AIMD-00-154, May 3, 2000).

IRS Modernization: Business Practice, Performance Management, and Information Technology Challenges (GAO/T-GGD/AIMD-00-144, Apr. 10, 2000).

IRS Restructuring Act: Implementation Under Way but Agency Modernization Important to Success (GAO/T-GGD-00-53, Feb. 2, 2000).

Financial Audit: IRS' Fiscal Year 1999 Financial Statements (GAO/AIMD-00-76, Feb. 29, 2000).

IRS Employee Evaluations: Opportunities to Better Balance Customer Service and Compliance Objectives (GAO/GGD-00-1, Oct. 14, 1999).

IRS Management: Formidable Challenges Confront IRS as It Attempts to Modernize (GAO/T-GGD/AIMD-99-255, July, 22, 1999).

Tax Systems Modernization: Results of Review of IRS' Initial Expenditure Plan (GAO/AIMD/GGD-99-206, June 15, 1999).

Tax Administration: IRS' 1999 Tax Filing Season (GAO/GGD-00-37, Dec. 15, 1999).

Tax Administration: IRS' 1998 Tax Filing Season (GAO/GGD-99-21, Dec. 31, 1998).

Tax Systems Modernization: Blueprint Is a Good Start But Not Yet Sufficiently Complete to Build or Acquire Systems (GAO/AIMD/GGD-98-54, Feb. 24, 1998).

Customs

U.S. Customs Service: Observations on Selected Operations and Program Issues (GAO/T-GGD/AIMD-00-150, Apr. 20, 2000).

U.S. Customs Service: Better Targeting of Airline Passengers for Personal Searches Could Produce Better Results (GAO/GGD-00-38, Mar. 17, 2000).

Customs Service Modernization: Serious Management and Technical Weaknesses Must Be Corrected (GAO/AIMD-99-41, Feb. 26, 1999).

Customs Service Modernization: Impact of New Trade Compliance Strategy Needs to Be Assessed (GAO/GGD-00-23, Dec. 15, 1999).

Customs Service: Process for Estimating and Allocating Inspectional Personnel (GAO/GGD-98-107, Apr. 30, 1998).

Financial Management

Financial Management Service: Significant Weaknesses in Computer Controls (GAO/AIMD-00-305, Sept. 26, 2000).

Debt Collection: Treasury Faces Challenges in Implementing Its Cross-Servicing Initiative (GAO/AIMD-00-234, Aug. 4, 2000).

Federal Reserve Banks: Areas for Improvement in Computer Controls (GAO/AIMD-00-218, July 7, 2000).

Observations on the Department of the Treasury's Fiscal Year 1999 Performance Report (GAO/GGD/AIMD-00-231R, June 30, 2000).

Debt Collection: Treasury Faces Challenges in Implementing Its Cross-Servicing Initiative (GAO/T-AIMD-00-213, June 8, 2000).

Financial Audit: 1999 Financial Report of the United States Government (GAO/AIMD-00-131, March 31, 2000).

Financial Audit: Bureau of the Public Debt's Fiscal Years 1999 and 1998 Schedules of Federal Debt (GAO/AIMD-00-79, March 1, 2000).

Financial Management Service: Significant Weaknesses in Computer Controls (GAO/AIMD-00-4, Oct. 4, 1999).

Federal Debt: Debt Management in a Period of Budget Surplus (GAO/AIMD-99-270, Sept. 29, 1999).

Financial Audit: Issues Regarding Reconciliations of Fund Balances with Treasury Accounts (AIMD-99-271, Sept. 17, 1999).

Federal Reserve Banks: Areas for Improvement in Computer Controls (GAO/AIMD-99-280, Sept. 15, 1999).

Federal Debt: Answers to Frequently Asked Questions—An Update (GAO/OCG-99-27, May 28, 1999).

Financial Audit: 1998 Financial Report of the United States Government (GAO/AIMD-99-130, Mar. 31, 1999).

ATF

Observations on the Department of the Treasury's Fiscal Year 1999 Performance Report and Fiscal Year 2001 Performance Plan (GAO/GGD/AIMD-00-231R, June 30, 2000).

Asset Forfeiture

Asset Forfeiture: Noncash Property Should Be Consolidated Under the Marshals Service (GAO/GGD-91-97, June 28, 1991).

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

Performance and Accountability Series

Major Management Challenges and Program Risks: A Governmentwide Perspective (GAO-01-241)

Major Management Challenges and Program Risks: Department of Agriculture (GAO-01-242)

Major Management Challenges and Program Risks: Department of Commerce (GAO-01-243)

Major Management Challenges and Program Risks: Department of Defense (GAO-01-244)

Major Management Challenges and Program Risks: Department of Education (GAO-01-245)

Major Management Challenges and Program Risks: Department of Energy (GAO-01-246)

Major Management Challenges and Program Risks: Department of Health and Human Services (GAO-01-247)

Major Management Challenges and Program Risks: Department of Housing and Urban Development (GAO-01-248)

Major Management Challenges and Program Risks: Department of the Interior (GAO-01-249)

Major Management Challenges and Program Risks: Department of Justice (GAO-01-250)

Major Management Challenges and Program Risks: Department of Labor (GAO-01-251)

Major Management Challenges and Program Risks: Department of State (GAO-01-252)

Major Management Challenges and Program Risks: Department of Transportation (GAO-01-253)

Major Management Challenges and Program Risks: Department of the Treasury (GAO-01-254)

Major Management Challenges and Program Risks: Department of Veterans Affairs (GAO-01-255)

Major Management Challenges and Program Risks: Agency for International Development (GAO-01-256)

Major Management Challenges and Program Risks: Environmental Protection Agency (GAO-01-257)

Major Management Challenges and Program Risks: National Aeronautics and Space Administration (GAO-01-258)

Major Management Challenges and Program Risks: Nuclear Regulatory Commission (GAO-01-259)

Major Management Challenges and Program Risks: Small Business Administration (GAO-01-260)

Major Management Challenges and Program Risks: Social Security Administration (GAO-01-261)

Major Management Challenges and Program Risks: U.S. Postal Service (GAO-01-262)

High-Risk Series: An Update (GAO-01-263)

Ordering Information

The first copy of each GAO report is free. Additional copies of reports are $2 each. A check or money order should be made out to the Superintendent of Documents. VISA and MasterCard credit cards are accepted, also.

Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:
U.S. General Accounting Office
P.O. Box 37050
Washington, DC 20013

Orders by visiting:
Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC

Orders by phone:
(202) 512-6000
fax: (202) 512-6061
TDD (202) 512-2537

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (202) 512-6000 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

Orders by Internet:
For information on how to access GAO reports on the Internet, send an e-mail message with "info" in the body to:

info@www.gao.gov

or visit GAO's World Wide Web home page at:

http://www.gao.gov

To Report Fraud, Waste, or Abuse in Federal Programs

Contact one:

- **Web site: http://www.gao.gov/fraudnet/fraudnet.htm**
- **e-mail: fraudnet@gao.gov**
- **1-800-424-5454 (automated answering system)**

PRINTED ON RECYCLED PAPER

United States
General Accounting Office
Washington, D.C. 20548-0001

Official Business
Penalty for Private Use $300

Address Correction Requested

Bulk Mail
Postage & Fees Paid
GAO
Permit No. GI00