

OVERSIGHT OF HIGH-RISK GOVERNMENT PROGRAMS

HEARING

BEFORE THE

COMMITTEE ON THE BUDGET HOUSE OF REPRESENTATIVES

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OVERSIGHT OF HIGH-RISK GOVERNMENT PROGRAMS

THURSDAY, FEBRUARY 17, 2000

HOUSE OF REPRESENTATIVES,
COMMITTEE ON THE BUDGET,
Washington, DC.

The committee met, pursuant to notice, at 10:08 a.m. in room 210, Cannon House Office Building, Hon. John R. Kasich (chairman of the committee) presiding.

Present: Representatives Kasich, Chambliss, Nussle, Hoekstra, Gutknecht, Sununu, Knollenberg, Thornberry, Miller, Ryan, Toomey, Spratt, Rivers, Bentsen, Davis, Clayton, Price, Markey, Clement, Moran, Lucas, and Holt.

Chairman KASICH. The committee will come to order, and we are pleased today to have with us the Comptroller of the GAO and a number of inspectors general.

I believe that this is going to start a series of hearings where we will be looking at the management of the Government. I told Mr. Spratt the other day—I really want everyone to understand. I didn't want to do this because I am interested, frankly, in any partisan gain or any fingerpointing from a partisan point of view. Just so people know, this is starting my 18th year in Congress, and the first 4 years I was here, I really was involved in major reform of the Pentagon, including the spare parts investigation and a number of other investigations, payments of contractors, and the way they billed. At that time, I made an awful lot of friends among the Republican administration. And then I think as most people here know, I worked with my great friend, Ron Dellums, to kill the only major weapons system that was killed in the 20th century by the Congress, and that was the B-2 bomber.

I am not interested in fingerpointing in any of this. I just think that we have a very big Government, and it is a Government that spends other people's money. And anytime you are spending other people's money, you are never going to be very cautious with it. It is just human nature. But I think it is the obligation of Members of Congress to do everything they can to make sure that we are as efficient as we can be.

I am fairly well convinced that what happens at the Pentagon and the problems that we saw, as I talked to Dave Walker, since when George Washington commanded the Continental Army, and the Army sold food supplies to contractors that were spoiled, there is always going to be waste, inefficiency, and things that make you want to pull out your hair.

In fact, I think it was Forrester who went over there to try to change the Pentagon, and he jumped out of the window before he finished—it was so difficult. And when you think about all the people that attended to that building, including people like David Packard, it is really a tremendous challenge. And every once in a while you have got to get in there and beat the bushes.

John, I don't know, this was a screw that was purchased in 1998 under that system where the DLA uses contractor catalogues to make purchases. This is a 57-cent item for which the Pentagon paid \$75.60.

Now, I started talking about this in 1983, and in 1998, we made a purchase like this. I am still sure that we are buying—I actually saw a specification for a whistle and how to blow that whistle. You emit a steady stream of air which makes the ball go around which brings out a shrill sound. That is how we buy whistles—we used to buy whistles in the Pentagon. I don't know if we are still doing it like that, but I suspect that we are.

We are going to look at four of the areas that we are finding as high risk here today, and we hope we are going to continue to pursue this. And we want to invite all the members to participate. This is not just going to be one effort, I hope, that will disappear.

We also have a website at the committee, and we have had lots and lots of hits on it. But I think we are in the neighborhood of several hundred items that we think the IGs have viewed as very legitimate. And I would hope at some point we could ask employees of the Federal Government to be able to testify anonymously. We have to figure out a system to be able to do that.

But I just really want everybody to know that this is not designed to be a political exercise. This is designed to try to honestly improve systems and learn. And when we take a look at Medicare, for example, and we find out that there are 900—think about this—900 million claims a year on Medicare, and the Federal Government hands its checkbook to a bill payer and says pay my bills, now you tell me of the 900 million claims that are reported that there is any sense that we really are getting our money's worth. There is a systemic problem in a system where the consumer is so far removed from the purchasing.

But enough from me. I hope that the members will find this interesting. I look forward to hearing from Mr. Walker. I have had a long relationship with the GAO. I can remember back probably 15 years ago, 14 years ago, when Republicans were attacking the General Accounting Office, and I went to the floor and defended them because I had always felt as though the GAO was willing to treat the lowest Member, newest Member of Congress as effectively as they treat the Speaker of the House or the Senate Majority Leader. And Mr. Walker is new in this job, relatively new in this job, and I believe he has a commitment to go back and shake up the GAO, because even organizations like that get stale and tired.

It is very important that our investigators are robust and that they are excited about their work, and I am very hopeful that Mr. Walker is going to be able to breathe some new life into this organization. He is a professional, I think a friend of Connie Mack, and is from Atlanta, Georgia. So I am looking forward to working with

Mr. Walker for my remaining time in the Congress, and I want to wish him the best of luck.

I would like to recognize Mr. Spratt for whatever comments he may have.

Mr. SPRATT. Thank you, Mr. Chairman. And to Mr. Walker, the Comptroller General, and our other witnesses, welcome. We are glad to have you participate in the hearing today, and we appreciate the substantial amount of work you have done to prepare for this.

This is an old staple. If there is one thing that Congress doesn't do as well as it should—and there are probably many things, oversight is one. It is clearly an area where we need to do more work, and this committee itself should be doing it along with the other committees which have that function and jurisdiction.

While we are doing it, we ought to look at ourselves. To be credible with the American people, to be fair to those whom we are criticizing, and, in fact, to root out waste, fraud, and abuse, we ought to look at our work product. We ought to look at the some of the earmarks in the appropriation reports that come out of here and ask ourselves if that is an efficient and un wasteful way of doing business.

We should look at some of the rules and regulations we prescribe for procurement. We should follow up on some of the laws that we have written that haven't been fully implemented. One is the chief financial officers law that requires the Congress, which imposed that particular requirement on the executive branch, to hold the feet to the fire of the different departments to see that they do that right.

Your predecessor, Mr. Walker, was a big believer in that and wanted to see each department develop what you might call an annual financial report. And each department is supposed to be doing that. It is not easy to do. You don't necessarily have systematic consistency in all your financial reports, but I think it is a worthy goal for the Federal Government annually to be able to come up with an annual report, assets, liabilities, income, outgo, exactly what you have done, and accrued liabilities, accrued future liabilities.

One of the things we don't do well in any part of the Government is variance analysis. Years ago we created something called the Selected Acquisition Report in the Defense Department. We tried to baseline performance, baseline schedule, and baseline cost, and then measure against that baseline over the life of the program.

That program has not evolved with time. It hasn't improved with time. And we don't have good systems for tracking the consistency of performance, scheduling, and cost in DOD, DOE, and lots of Government departments, NASA, too, I am sure.

Just a couple of caveats, and then I think we need to start the hearing because a lot of members will need to be getting out of here, and the witnesses will, too.

First of all, we are talking about waste, fraud, and abuse. A lot of what we are talking about is not fraud, and the American people should understand that. It gets grouped under that rubric, but, for example, Medicare. HHS has reported substantial overpayments. They found more overpayments as a result of improper payments

as a result of the fact that we have given them more money to be more vigilant and more inquisitive about how they are being billed and what they are actually paying.

A very, very small percentage of this is true fraud. Much of it is simply improper billing, billing the wrong thing or in some cases paying the wrong thing from the wrong account.

Secondly, there are a lot of things that get dredged up that simply aren't true. A lot of the old canards about defense procurement excesses turn out really to be exaggerations, they weren't that true, and that is why nothing ever happens here. We go off in pursuit of these red herrings that really turn out not to be that valid after all.

Then, finally, as I said, we really ought to take a look at ourselves and the extent to which we contribute to this problem in the appropriations process and the authorization process and, in fact, that we do oversight, but it is a lot of jawboning that tends not to be followed up very effectively. Once we get through pronouncing it, it is left in a report somewhere.

Here is a report, for example, a majority staff report, Committee on Government Operations, my committee, "Managing the Federal Government: A Decade of Decline," printed in 1993. And it is full of apparent waste, fraud, and abuse. And I daresay if we looked into this manual, we would find many of the things cited here still being practiced today. Some have been corrected. Some haven't been. And some, as I said, weren't problems in the first place. They were simply cited as such because of a lack of understanding.

We appreciate you witnesses coming today because we need to tell the American taxpayers, they are not paying anything more than necessary to get the Government they deserve. And we have to maintain continual oversight to see that that is the case. We sit sort of as a board of directors, and we appreciate the assistance you are providing us today, and we look forward to your testimony.

Thank you very much.

**STATEMENT OF DAVID M. WALKER, COMPTROLLER GENERAL,
UNITED STATES GENERAL ACCOUNTING OFFICE**

Mr. WALKER. Thank you, Mr. Chairman and Mr. Spratt. Members of the committee, it is a pleasure to be here.

Mr. Chairman, as you and I agreed by phone, I am going to talk probably about 20 minutes because I want to give you some meat including some specific examples in order to bring some of these issues to life.

I very much appreciate the opportunity to be before you this morning on behalf of the General Accounting Office to discuss our views on targets of opportunity for you and other Members of Congress to consider in order to maximize the performance, ensure the economy, and assure the accountability of the Federal Government for the benefit of the American people.

This committee is to be commended for holding these hearings and emphasizing that, surplus or no surplus, poor performance, waste, and inefficiency in Government cannot be ignored. No matter how large the projected surpluses may be, they do not absolve the Government of its responsibility to pursue fraud, waste, abuse, and inefficiency and to make prudent use of taxpayer dollars.

We also have an obligation to modernize Government to more effectively address the needs of our changing society. Many of our current Federal programs—their goals, organizations, and processes—were designed decades ago. Given this context, it shouldn't be insulting nor threatening to any Federal program or activity to question their relevance or fit in today's world. In fact, it is wholly appropriate and prudent to do so. This is especially important given the long-range budget challenges we face stemming from our aging society and the known approaching demographic tidal wave, which will hit.

The first chart, which is on my left, lists examples of Federal programs and operations that, based upon our past work, warrant reexamination for one of three major reasons: first, to improve the economy and efficiency of existing Federal operations; secondly, to reassess what the Government does; and, thirdly, to redefine the beneficiaries of Federal Government programs. These are illustrative. We have others. But for time and space considerations, we wanted to focus on these.

I will review several examples of these after I discuss our high-risk series. Our high-risk series is noted on the right, the results of our latest high-risk report which, as you know, ladies and gentlemen is done every 2 years. Our latest report came out in January of 1999.

Over the years, our work has shown that various functions and programs critical to personal and national security, ranging from Medicare and housing to tax administration and weapons acquisitions, have been hampered by significant and recurring financial and management program problems that expose these activities to increased risk of fraud, waste, abuse, and inefficiency.

Successfully addressing these problems offers the potential to achieve major savings over time through improved services to the public and hopefully will also serve to, in addition to improving the economy, improve the public's respect for and confidence in their Government over time.

In January 1999, GAO updated our high-risk series. The latest update includes 26 programs that are vulnerable to higher levels of fraud, waste, abuse, or other activities. Six areas have been removed since we began our series in 1990 while 10 of the original areas remain on the list.

We have also recently issued a report identifying the range and magnitude of improper payments, and as Mr. Spratt pointed out, that does not necessarily mean fraud. And I will clarify that later—improper payments from Federal programs based upon agency estimates and their financial statements, many of which relate to these high-risk areas.

In my written settlement, which is extensive—and I would commend it to you and your staff—we discuss selected high-risk and improper payment areas along with case examples from GAO and inspector general reports to demonstrate how the underlying management and program design problems can result in waste and poor performance.

I would now like to discuss some examples to put a face on some of these issues within the time allowed.

First, Medicare. With annual payments of about \$200 billion, Medicare is one of the fastest-growing major social programs in the Federal budget, and it is expected to almost double in size in the next 10 years alone. Importantly, the demographic tidal wave that I mentioned won't hit until 2011. Medicare's problems really escalate after that.

Medicare finances health care services delivered by hundreds of thousands of providers to tens of millions of beneficiaries. This program has been a perpetually attractive target for exploitation. People go where the money is, requiring constant vigilance and increasingly sophisticated approaches to protect the system from wrongdoing and abuse.

HHS has begun to identify improper payments, that is, payments made in error. Based on the financial statements for the \$176 billion Medicare fee-for-service program, between the years 1996 and 1998, the estimated total annual payments made in error in this program dropped from \$23.2 billion to \$12.6 billion. But that is still a lot of money.

Sources of these errors included payments unsupported by documentation, payments made for unnecessary medical procedures, incorrectly coding billing for services, or upcoding—trying to code for higher levels of services than were actually provided—and payments for unallowable services. The reductions in erroneous payments were largely attributable to better claims documentation by providers rather than a reduction in the other three categories. Moreover, this estimate does not include all losses due to fraudulent schemes, such as collusion, kickbacks, and false claims for services not provided.

Problems with abuse in this system partially stem from the program's oversight structure. HCFA delegates the review of claims to its contractors, yet its oversight of these contractors does not provide adequate assurance that claims are properly paid.

In our written statement, we highlight the case of a major Medicare contractor who settled a \$140 million claim and pled guilty to eight felony counts for, among other things, rushing payments through the payment system by shutting off the computer edits designed to avoid improper payments, allowing Medicare to make payments for claims that should have been made by private insurers—as you know, Medicare is a secondary payer—and disconnecting toll-free phone lines used for beneficiary inquiries and complaints.

Medicare has proven to be vulnerable to fraud by career criminal and organized crime elements posing as health care providers. These groups have created sham medical clinics or other entities or used the names of legitimate providers to bill for services either not provided or medically unnecessary.

For instance, the rent-a-patient scheme. In two South Florida cases, recruiters organized thousands of beneficiaries from, among other places, retirement communities and drove them to area clinics for rote examinations and unnecessary testing and treatment. Recruiters received a fee that they shared with the beneficiaries. It could be referred to as a kickback. It may have been knowing or unknowing. Beneficiaries understood that they should go elsewhere if they needed a real doctor.

Several licensed physicians participated in the scheme in which they signed medical records for services they neither performed nor supervised. The clinics then billed Medicare, Medicaid, and other private insurers for services either not necessary or not performed. In one or two of the cases, the clinics filed over \$120 million in fraudulent Medicare claims and \$80 million was paid. The leaders of the ring were arrested and sentenced to prison for health care fraud and are now wearing wide-striped suits.

Other improper payments. Mr. Chairman—

Chairman KASICH. May I just interrupt you briefly there?

Mr. WALKER. Yes, Mr. Chairman.

Chairman KASICH. My understanding is that the estimates we have that involve improper billing, fraud, or whatever, does not include these dummy practices, i.e., people who claim to be doctors who are not doctors, who have patients—claim to have patients where there are no patients. Is that correct?

Mr. WALKER. It does not include all forms of fraud and collusion, including some practices that you just articulated. And I am sure that the IG for HHS, June Gibbs Brown, can give you more detail on what their methodology does and does not include. Thank you, Mr. Chairman.

Other improper payments. Many other Federal programs, in addition to Medicare, are vulnerable to improper payments. The Federal Government's fiscal year 1998 financial statement reports from nine agencies alone estimated that improper payments amounted to \$19.1 billion. In addition to the Medicare program, this estimate included improper payments from such programs as Social Security, \$1.2 billion; food stamps, \$1.4 billion; housing subsidies, \$857 million; and Supplemental Security Income, \$1.6 billion.

Importantly, the amount of improper payments is greater than that disclosed thus far in agency financial statements. In addition, audit reports from GAO and agency inspectors general have identified other agencies that have made improper payments but did not include estimates in their financial statements or have yet to do so.

For instance, as you mentioned, Mr. Chairman, HHS has not estimated improper payments for the Medicaid program which has \$108 billion in Federal outlays for fiscal year 1999. Our recent work has concluded that the size and structure of this program makes it inherently subject to exploitation.

Common Medicaid fraud and abuse schemes fall into three broad groups; improper billing practices, misrepresentation of professional qualifications and improper business practices such as kickbacks, self-referrals or collusion. In one case, two businesses netted \$10 million in excess Medicaid payments related to phony contracts with nursing homes to a shell company.

Illicit diversion of Medicaid-covered prescription drugs has also proven to be a persistent problem. Schemes include pharmacists who routinely add drugs to legitimate prescriptions and keep the extra amount for sale to others, and individuals who provide recipients with controlled substances in exchange for subsequent illicit use of their Medicaid recipient numbers.

We have recommended that OMB develop guidance for agencies to help them estimate improper payments more systematically for Federal programs and to prompt them to develop goals to address

these issues in their annual performance plans in consultation with appropriate congressional oversight committees. OMB has started to work with the agencies to develop guidance to assist agencies in doing this. This needs to be a high priority, not just within the executive branch but also for congressional oversight.

HUD programs—

Chairman KASICH. Could I just stop you there with Medicaid?

Mr. WALKER. Yes, Mr. Chairman.

Chairman KASICH. Is it fair to assume that the Medicaid program really has not been reviewed? Is that correct?

Mr. WALKER. It hasn't been as extensively reviewed as the Medicare program, at least as it relates to some of these estimation techniques, and more needs to be done in that area.

In 1994, we designed HUD programs as a high-risk area because of our work and that of others, such as the HUD inspector general. We identified four serious, longstanding departmentwide management problems that, taken together, placed the integrity and accountability of several major HUD programs at high risk. These deficiencies included weak internal controls, an ineffective organizational structure, an insufficient mix of staff with the proper skills, and inadequate information and financial management systems.

We concluded that while HUD had efforts underway to address the numerous and severe problems that frankly have occurred over years that have significant impact on program management, billions of dollars across most of the agencies' major programs continue to be at risk.

Our recent work demonstrates that HUD has made credible progress in addressing a number of these challenges, but significant challenges remain.

For instance, we noted in 1999 that inadequate monitoring and problems with information and financial management systems persist. HUD is likely to spend millions of dollars, miss milestones, and still not meet its objective of developing and fully deploying an innovative financial management system because it has not yet finalized detailed plans of how to do this.

In 1998, we have reported weaknesses in HUD's oversight of its single-family inventory, which are properties acquired by HUD and managed by contractors when borrowers default on single-family mortgages insured by HUD. Our physical inspection of selected properties identified serious problems with vandalism, maintenance problems, and safety hazards that may have decreased marketability, increased HUD's holding cost, and in some instances threatened the health and safety of neighbors and potential buyers.

In my written statement, we discuss the case of one contractor responsible for 40 percent of HUD's workload whose failures to adequately maintain these properties or make them available for sale prompted to HUD to properly terminate that contractor, ultimately leading to the contractor's bankruptcy filing, at the same point in time it created a major void with regard to the administration and oversight of these programs.

Since 1995, HUD has taken a number of actions to address its management deficiencies, and it has made credible progress. For example, the Department has improved its financial reporting and received an unqualified opinion for the fiscal year 1998 financial

statements. In our 1999 high-risk series update, we noted that HUD's Secretary and leadership team have given a top priority to addressing the Department's management deficiencies. A major factor in HUD's progress has been the June 1997 2020 Management Reform Plan, which called for reducing the number of programs, retraining staff, reorganizing the field offices, consolidating processes and functions into specialized centers, and modernizing and integrating information and financial management systems.

While comprehensive plans to address such problems represent a positive step forward, ultimately it is results that count. We are monitoring HUD's progress, and it is too soon to tell whether these reforms will be successfully implemented in order to sufficiently address these problems in conjunction with over the long term as well as our next high-risk series update.

DOD management. Six of our current 26 high-risk areas relate to longstanding DOD management problems. The Department's size, culture, and organizational structure present major management challenges.

While DOD is clearly number one in the world in fighting and winning armed conflicts, it is a D-plus in the area of economy and efficiency, although they are showing signs of taking this much more seriously and have started to make some progress.

With regard to financial management, no major part of DOD is able to pass the test of an independent financial statement audit. Many have trouble just putting together a financial statement, much less having an audited financial statement. The absence of integrated financial management systems has hampered the agency's ability to prepare financial statements and engage in sound day-to-day management practices.

The continuing financial management problems have real consequences for program management and resource allocation. For instance, DOD cannot properly account for billions of dollars of basic transactions, leaving the agency vulnerable to the misuse of appropriated funds.

For example, auditors reported that the Air Force depot management activity, a component of one of the Department's working capital funds, may have obligated \$1.1 billion more than it had available as of September 30, 1998. In addition, DOD's records do not consistently reflect the number and location of its inventories and weapons systems, increasing the risk that inventory managers may request funds for items that are already on hand. In addition, it may make it difficult in order to be able to use items that are needed because they don't know where they are when they are needed.

Contract management. DOD continues to overpay contractors. While the full extent of overpayments is unknown, we do know that between fiscal year 1994 and 1998, defense contractors returned voluntarily \$4.6 billion in overpayments, an average of about \$920 million a year. Surprisingly, under current law, there is no requirement for contractors who have been overpaid to notify the Government, much less to send the money back. And, in fact, there aren't even any incentives for them to do so or penalties if they don't.

Weapons system acquisitions. DOD spends over \$80 billion annually to research, develop, and acquire weapons systems. Although

DOD has many acquisition reform initiatives in process, fundamental weapon system problems persist. These systemic problems serve to reduce the system's performance and waste taxpayer dollars.

The competition for funding when a program is launched within DOD encourages aspiring DOD programs and their managers and sponsors to include performance features that rely upon immature technologies and overly ambitious cost and schedule estimates. For example, the Comanche helicopter. That development program is being restructured for the fifth time in the last 10 years due to uncertain and changing requirements and unattainable cost and schedule estimates. This latest restructure/development plan still contains significant risks of further cost overruns, schedule delays, and degraded performance. Annual production costs are now projected to be over \$2 billion by the year 2008—\$2 billion a year. This will comprise about 64 percent of the army's aviation budget over time.

Now, I can assure you this picture is not the Comanche helicopter, but this is relevant to the next illustration I would like to provide.

These problems also exist in noncombatant systems. For example, the Army has procured thousands of high-mobility trailers, which you see on my right, that are not usable or suitable. It awarded this multiyear production contract without first demonstrating that the design would meet its requirements.

I wanted to bring a trailer and tow it up here and park it outside for you to be able to see one of these. However, the picture is going to have to do because it proved to be inappropriate. We have thousands in storage. The trailers are found to damage the trucks that tow them. Moreover, the Army found that the trailer draw bar could break, causing the trailer to overturn, disconnect, causing damage to property and possibly to persons as well. Therefore, I did not think it would be prudent for us to attempt to pull one up here.

Believe it or not, the Army has procured 6,700 of these at a current price of over \$10,000 each. Unfortunately, this is the rule rather than the exception in connection with many DOD acquisition programs.

Now, let me clarify here, Mr. Chairman and members. They are going to be able to fix this. It is going to cost a thousand bucks, or so to fix it, and it is going to take time, and they want to procure another, you know, probably 18,000 of these eventually. But this is a systemic problem. And one of the major concerns that I have about procurement and acquisitions, especially in DOD, is they do not follow proven commercial best practices for acquisitions.

Now, I can understand that in a circumstance where we have a credible national security threat. I do not understand that at all in a circumstance where we don't. The current approach results in systems, whether they be combatant or noncombatant, not meeting performance requirements, significant delays, and billions—billions—of wasted money that maybe should go to defense but could be reallocated to more critical needs like readiness and other areas, because we already know that we have a tremendous squeeze coming on the defense budget based upon known budget projections and restrictions on discretionary spending.

Reducing and resolving risk in Federal programs. To be fair, several Federal agencies have taken many of these high-risk programs seriously and are making progress in addressing them. Congress has also acted to provide oversight and needed legislative changes in connection with a few of these issues. However, more needs to be done by both the executive branch and the Congress to accelerate progress in these areas. Many of these problems have existed for years. They are deeply rooted, complex, and persistent and sustained attention by both the executive branch, including OMB, as well as the Congress will be needed in order to achieve lasting improvement.

Some areas may, in fact, require targeted legislative action or modest investment in information or financial systems and human capital initiatives in order to achieve the savings or increased performance.

Plans have been conceived to address many of these issues, but the more difficult implementation task of translating these plans into day-to-day management reality lies ahead for many of these areas. Vigilant congressional oversight will be absolutely critical to promoting and sustaining the high-level focus that is necessary in order to resolve these problems.

High-risk areas and improper payment problems reflect deeply rooted weaknesses in Federal financial and program management systems and controls. The Government's financial systems are often unable to perform the most basic bookkeeping requirements for Federal entities, many of which are engaged in financial transactions whose magnitude, complexity, and risk exceeds those experienced by the largest global private sector enterprises. After all, the United States is the largest, most complex, most diverse entity on the face of the Earth bar none, public or private sector.

The agency's inability to account for substantial liabilities, assets, net costs, or improper payments were among the factors that prevented us from being able to form an opinion on the Government's consolidated financial statements for the 2 years that we have been performing this audit. They will also prevent us from rendering an opinion on the fiscal year 1999 consolidated financial statements, and we are likely not to be able to render an opinion on these statements until several key issues are addressed, in particular DOD's financial management systems.

I do not believe we will ever be able to express an opinion without DOD getting its act together, and they project that that will not happen until 2003 at the earliest, although they are trying and they are making some progress.

Agencies have made uneven progress in obtaining clean financial statement opinions; however, even where this important milestone has been reached—

Chairman KASICH. Wait, wait.

Mr. WALKER. Yes, Mr. Chairman.

Chairman KASICH. I don't want to miss—are you trying to tell me that you can't audit the DOD books until 2003?

Mr. WALKER. Let me clarify, Mr. Chairman. They are being subject to audit. What I am saying is that we at GAO are the auditors of the consolidated financial statements of the Federal Government. At the present time, the inspector general audits DOD, and

then we review the work that they do in order to determine the impact on our audit of the overall Government.

What I am saying is that the IG has not been able to express an opinion on DOD, and unless and until they can do that, we are not going to be able to express an opinion on the overall Government. DOD doesn't believe they are going to be in shape to achieve that objective until, at the earliest, 2003. And so they are still being subject to audit; however, the problems are so embedded, they are so systemic, and they are so significant that the executive branch is estimating it is going to take them at least 3 years to get to that point.

Mr. SPRATT. Wouldn't you agree that DOD is subject to more continual internal audit because of the Defense Contract Agency than most other Government departments?

Mr. WALKER. They have a number of oversight entities. They have DCAA. They have the different service internal auditors, if you will. They also have the overall inspector general for DOD as well. And so it is not that they are not subject to oversight.

Candidly, as I said before, Mr. Spratt, DOD is an A, number one in the world in performance and results on the battlefield. But, frankly, they didn't focus for decades on economy and efficiency, and they are just now starting to really focus on it. But there is a lot more that needs to be done there because we are talking about a lot of money.

Agencies have made uneven progress in obtaining these clean opinions. But even when this important milestone has been reached—and as you know, 12 of the 24 major departments and agencies received clean opinions on their 1998 financial statements. The executive branch is hopeful that 18 will for 1999. I think that might be optimistic. But the fact of the matter is, even when they reach this important milestone of getting a clean opinion, that is not the end, because the purpose of the CFO Act is to make sure that Government agencies and their management have timely, accurate, useful information to make informed management decisions day to day. And, in fact, what has happened in the case of some of these agencies who have gotten clean opinions, they have hired outside contractors, spent millions of dollars in order to be in a position to get a clean opinion on their financial statements, months after the end of the year, and yet their systems are such for them to manage their operations effectively during the year. That is not what we should be doing here.

You know, getting a clean opinion is an important milestone. We ought to do it. But that is not the end game. We have got to focus on dealing with the fundamentals.

Mr. Chairman, the deep-seated nature of many of these high-risk areas does not mean that they are immutable. In fact, we have noted significant improvements in several areas. For example, where a partnership approach is employed—by that I mean where the Congress takes this seriously and where the executive branch takes this seriously—progress can and has been made. The U.S. Customs Service was removed from our high-risk list last year due to consistent progress in addressing major management and organizational weaknesses. Coupled with a major reorganization, the agency has made major improvements in its financial management

and enforcement of the Nation's trade laws. Sustained management commitment and congressional oversight was essential for this progress.

In this regard, the agencies' initiatives received important and consistent backing and reinforcement during this period from the Results Caucus, commissioned by the House leadership.

Mr. Chairman, if I can go briefly on the rest, I am going to try to summarize the rest, that is high-risk, but I do want to talk a little bit about these three categories. And I would like to give you one example, if I can, of each of these categories.

In addition to overseeing high-risk areas, numerous other opportunities are available to focus congressional oversight and improve Government efficiency, modernize operations, update priorities, and target Federal payments and subsidies. Our written statement has numerous examples. I am going to provide one example of each major category.

With regard to improving economy and efficiency, congressional reviews can focus on opportunities such as consolidation or coordination of programs with similar objectives and the reengineering and streamlining of Federal processes. One example involves a Federal system to ensure the safety and quality of our Nation's food system.

The current system is inefficient and outdated. It suffers from overlapping and duplicative inspections, poor coordination, inefficient allocation of resources, and inadequate recovery of costs.

For example, the USDA Food Safety and Inspection Service is responsible for the safety of meat pizzas—and there are ten other Federal agencies that administer over 35 different laws that include food safety. So USDA has meat pizzas, but FDA has cheese pizza. And we have got a lot of players in the ball game here, and I think all of us can probably agree that food safety is important. It is important to all of us. But we need to go about it in a way that is efficient and effective.

Given this environment, the Congress could consider consolidating food safety agencies under the activities of a single agency in order to have a uniform set of food safety laws and enforcement activities.

The second area, reassessing what the Government does. It is important to periodically reexamine whether current programs and activities remain relevant, appropriate, and effective for our changing society. Our work demonstrates that congressional oversight could usefully address such fundamental questions as whether changing conditions have rendered particular programs obsolete or in need of major reform. After all, a lot of these programs started decades ago when there was a bona fide need that wasn't being met by the private sector or State and local governments. But what has happened over the years is they get in the baseline. So it is presumed that that need still exists, and it is also presumed that they are effectively meeting that need. In some cases, that is true, but not in all.

And I think now that we are entering the 21st century and now that we have time and don't have to focus on annual deficits, we don't have to focus on the Cold War, we have got an opportunity to take a more comprehensive view and to reassess what is the role

of Government, what should it be, and how can we best achieve what those desired objectives are.

The USDA Market Access Program is a case in point. This program subsidizes a portion of U.S. agricultural products in overseas markets. Despite changes made to the program between 1993 and 1998, serious questions remain over its results, including whether subsidized promotions generate positive net economic returns to the United States, increase exports that would have not otherwise occurred, and supplement rather than supplant private sector spending. Moreover, MAP promotions can have significant unintended effects.

For example, a 1996 study of U.S. apple exports in the United Kingdom and Singapore found that the U.S. market share in export value increased in the United Kingdom, but that foreign competitors actually gained a lot more than the United States did in Singapore as a result of this program.

The last general topic: redefine who benefits from Federal Government programs. To better reflect changing conditions and target limited resources, Congress should periodically reexamine the eligibility rules and formulas for Federal subsidies to States, businesses, and individuals. As presently designed, a variety of grants, tax expenditures, loans, and loan guarantees provide subsidies to recipients who would have undertaken the activity without Federal subsidy and thus avoid bearing their fair share of risk and cost.

For example, repetitive flood loss is one of the major factors contributing to the financial difficulties facing the National Flood Insurance Program. Approximately 43,000 buildings currently insured under the National Flood Insurance Program have been flooded on more than one occasion. These repetitive losses account for 36 percent of all program claims historically, about \$200 million a year, even though the repetitive loss structure makes up a very small portion of the total insured population, only about 1 to 2 percent.

The cost of the program of these multiple-loss properties over the years has been about \$2 billion. The Congress and FEMA could consider eliminating flood insurance and emphasizing mitigation for certain repeatedly flooded properties, removing what some argue is now an incentive to locate in harm's way.

Mr. Chairman, trying to sum up here, I am sure that this list of Government performance and management problems is sobering. There is much that remains to be done, but the task is not overwhelming. This is an opportune time to reinvigorate congressional oversight because we are relieved from the burdens of annual deficits and, in addition, we don't have certain external challenges such as the Cold War environment to focus on. But to achieve positive and lasting results requires sustained effort and commitment not only behalf of the executive branch but also on behalf of the legislative branch.

As you know, making progress in this area can be a daunting challenge that involves tough work over a sustained period of time, and in many cases, quite frankly, it is not very sexy and it doesn't grab a whole lot of headlines. But as was pointed out previously, I think by Mr. Spratt, we collectively have a fiduciary responsibility to make sure that the taxpayer dollars are used efficiently and

effectively. We ultimately have a finite amount of resources, and we need to make sure that those resources are targeted to get the maximum return on the taxpayers' investment. And while we are rolling in dough right now, at least we think we are based upon projected budget surpluses, based upon our long-range budget simulations we show we are going to be in the soup again because of escalating costs associated with entitlement programs due to known demographic trends. So we really need to reinvigorate congressional oversight.

I commend you, Mr. Chairman, for holding these hearings and reminding us of the importance of continued diligence regarding performance, economy, and accountability of Government programs. We look forward to continuing to work with you, and I will mention—and I think it is important to say this—GAO is on the front line every day in this area. And you are getting a return on that investment. On average, GAO generates \$20 billion in annual financial benefits or a return on your investment and the taxpayers' investment of \$57 for every \$1 invested, number one in the world, bar none. And we look forward to working with you and addressing these and other issues.

Thank you, Mr. Chairman.

[The prepared statement of David Walker follows:]

PREPARED STATEMENT OF DAVID M. WALKER, COMPTROLLER GENERAL OF THE
UNITED STATES

I appreciate the opportunity to be here this morning to discuss our views on targets of opportunities that you and other Members of the Congress can consider when addressing the budget and oversight challenges before you. The Committee is to be commended for holding these hearings and emphasizing that—surplus or no surplus—poor performance, waste, and inefficiency cannot be ignored. No matter how large the projected surpluses may be, they do not absolve the government of its responsibility to make prudent use of taxpayer dollars. Rather, the surplus provides an opportunity to rise out of the 1-, 3-, or 5-year budget horizons of recent deficit debates and to focus on how to restore the public's trust and confidence in their government.

After a decade of deficit reduction, we know there are pent-up demands for using projected surpluses. However, if careful scrutiny is given only to new spending or tax proposals, policymakers will have missed a critical window to address known performance problems in government. Left unresolved, these problems can expose Federal programs and operations to unnecessary risk, excessive costs, and chronic performance shortfalls. Resolving some of these problems offers the potential to save billions of dollars and dramatically improve the delivery of services to the American public. For instance, nine Federal agencies estimated improper payments of \$19.1 billion for fiscal year 1998 and we continue to highlight 26 major areas as being highly vulnerable to fraud, waste, abuse, and mismanagement.

These persistent problems suggest that we cannot afford to be any less vigilant in our attention to programs at high risk of fraud, waste, abuse, and mismanagement in a time of surplus. In fact, it is our obligation to safeguard benefits for those that deserve them by preventing the diversion of scarce Federal resources for inappropriate, unauthorized, or illegal purposes. The activities that GAO has identified as high-risk areas warrant vigilant and persistent oversight and attention by executive agencies and the Congress alike. Significant opportunities exist to reduce waste and improve the economy and efficiency of Federal activities in other areas as well, as I will discuss in my statement today.

Mr. Chairman, we also have an obligation to modernize government to more effectively address the needs of a changing society. As we enter a new century, we have been reminded about how much things change. Yet many of our programs—their goals, organizations, and processes—were designed long ago. Given this context, it shouldn't be insulting or threatening to any Federal program or activity to question its relevance or "fit" in today's world. In fact, it is wholly appropriate and prudent to do so.

Examining the legacy of existing activities and programs can yield important benefits. First, we can provide for much needed flexibility to address looming cost pressures and emerging needs by weeding out wasteful and inefficient programs that have proven to be outdated and no longer relevant to our changing society. As the baby boom retires, enhancing budgetary flexibility will be even more critical as the projected growth of Social Security and health care outlays threaten to crowd out other priorities. Second, we can update and modernize those activities that remain relevant by improving their targeting and efficiency through such actions as redesigning formulas, enhancing cost sharing by beneficiaries, consolidating facilities and programs, and streamlining and reengineering operations and activities.

All of our work reaffirms that with billions of dollars at risk and notwithstanding our current budget surplus environment, the Congress and Federal agencies need to devote sustained attention to oversight and reexamination of existing programs and activities to improve the performance of government and reduce the potential for fraud, waste, abuse, and mismanagement. Let me hasten to add that Federal agencies have taken the high-risk areas seriously and are making progress in addressing them, and the Congress has also acted to provide oversight and needed legislative changes. However, more needs to be done by executive agencies and the Congress to accelerate progress. Many of these problems are deeply rooted and complex. Although plans have been conceived to address many of these issues, the more difficult implementation task of successfully translating those plans into day-to-day management reality lies ahead for many of these areas. Vigilant congressional oversight will be absolutely critical to promoting and sustaining a high level focus on these problems and support for appropriate actions to address them.

Mr. Chairman, I don't need to tell you that sorting through existing programs is a serious, if often unglamorous, task that is nonetheless vital. This task is made particularly difficult because existing programs and commitments are "in the base" in budgetary terms and can have an advantage over new initiatives and demands.

In my testimony today I draw on the full breadth of GAO work to highlight numerous examples of significant performance problems in Federal agencies and programs, each drawn from the key findings and issues developed in our audits and evaluations.¹ To facilitate our discussion, the examples are organized around the following four broad themes:

- Attack activities at risk of fraud, waste, abuse, and mismanagement: focus on minimizing risks and costs associated with the delivery of major Federal programs and activities.
- Improve the economy and efficiency of Federal operations: capture opportunities to reduce costs through restructuring and streamlining Federal activities.
- Reassess what the Federal Government does: reconsider whether to terminate or revise outdated programs or services provided.
- Redefine the beneficiaries of Federal Government programs: reconsider who is eligible for, pays for, and/or benefits from a particular program to maximize Federal investments.

ATTACKING ACTIVITIES AT RISK OF FRAUD, WASTE, ABUSE, AND MISMANAGEMENT

Mr. Chairman, in selecting priorities for oversight, major attention should be given to addressing the vulnerability of many critical Federal programs and operations to the risk of fraud, waste, abuse, and mismanagement. Over the years, our work has shown that central functions and programs critical to personal and national security, ranging from Medicare to weapons acquisitions, have been hampered by daunting financial and program management problems. These problems result in persistent exposure of these activities to waste and abuse.

These weaknesses have real consequences with large stakes that are important and visible to many Americans. Some of the problems involve the waste or improper use of scarce Federal resources: Federal funds are diverted from their intended uses or beneficiaries, revenues owed are not effectively identified or collected, or excessive inventories and procurement costs drive Federal costs higher than they need to be for some areas. Other problems compromise the ability of the Federal Government to deliver critically needed services: systemic information management weaknesses undermine the nation's ability to modernize our technology for tax processing, air-

¹ Many of the examples discussed in this testimony were developed as part of our annual effort to describe the budgetary implications of our work. See Budget Issues: Budgetary Implications of Selected GAO Work for Fiscal Year 2000 (GAO/OCG-99-26, Apr. 16, 1999). We expect to update and issue this product to this Committee and others next month and are currently working with the Congressional Budget Office and the Joint Committee on Taxation to develop estimates of budget savings or revenue gains for these and other examples.

line safety, and weather forecasting; and systemic procurement problems hamper the development of weapons systems and the cleanup of hazardous wastes at DOE sites. Perhaps of greatest importance is the impact of these problems on our ability to safeguard critical assets and operations from theft and misuse, whether it is critical national security information or private tax return information.

AREAS AT HIGH RISK AND PROGRAMS VULNERABLE TO IMPROPER PAYMENTS

In January 1999, we reported on specific Federal activities and functions that are particularly vulnerable to fraud, waste, abuse, and mismanagement—an update to a series on high-risk activities begun in the last decade and provided at the start of each new Congress.² Since 1990, six of our high-risk designations have been removed as a result of sustained, tangible improvements by the affected agencies; at the time of our last update, however, 26 high-risk areas remained, as shown in table 1. We have also recently reported on estimates of the range and magnitude of improper payments within specific Federal programs—several of which have also been identified as high-risk areas—as disclosed in agency financial statements reports.

TABLE 1.—1999 HIGH-RISK AREAS AND THE YEAR DESIGNATED*

High-risk area	Year
Reducing Inordinate Program Management Risks	
Medicare	1990
Supplemental Security Income	1997
Internal Revenue Service (IRS) Tax Filing Fraud	1995
Department of Defense (DOD) Infrastructure Management	1997
Department of Housing and Urban Development (HUD) Programs	1994
Student Financial Aid Programs	1990
Farm Loan Programs	1990
Asset Forfeiture Programs	1990
The 2000 Census	1997
Managing Large Procurement Operations More Efficiently	
DOD Inventory Management	1990
DOD Weapon Systems Acquisition	1990
DOD Contract Management	1992
Department of Energy Contract Management	1990
Superfund Contract Management	1990
National Aeronautical and Space Administration Contract Management	1990
Ensuring Major Technology Investments Improve Services	
Air Traffic Control Modernization	1995
Tax Systems Modernization	1995
National Weather Service Modernization	1995
DOD Systems Development and Modernization Efforts	1995
Providing Basic Financial Accountability	
DOD Financial Management	1995
Forest Service Financial Management	1999
Federal Aviation Administration Financial Management	1999
IRS Financial Management	1995
IRS Receivables	1990
Resolving Serious Information Security Weaknesses	
	1997

*Note: Our most recent update to the high-risk list in January 1999 also included "Addressing the Urgent Year 2000 Computing Challenge." Given the progress that has been made on this issue, we have not included it in this summary table. See Year 2000 Computing Challenge: Leadership and Partnerships Result in Limited Rollover Disruptions (GAO/T-AIMD-00-70, Jan. 27, 2000).

The high-risk areas shown in Table 1 as well as other improper payments reflect serious and continuing problems with financial, information, and program management across many Federal functions and agencies. Collectively, these areas affect almost all of the government's annual \$1.7 trillion in revenue and span critical government programs and operations from benefit programs to large lending operations, major military and civilian agency contracting, and defense infrastructure. Lasting solutions to these problems offer the potential to save billions of dollars, dramatically improve services to the public, and strengthen confidence in the accountability and performance of the national government.

In these areas, more needs to be done to achieve real and sustained improvements. GAO has made many recommendations to address and correct these prob-

²GAO has issued update reports on the status of high-risk areas every other year since 1993. Our latest report was High-Risk Series: An Update (GAO/HR-99-1, Jan. 1999).

lems. However, these problems will take time to fully resolve because they reflect deep-rooted, difficult problems in very large programs and organizations. Real improvements in performance and management will require persistent and sustained attention, and some areas may in fact need targeted and well-chosen investments in systems and human capital in order to achieve recurring savings.

I will now turn to a discussion of selected areas, which illustrate the problems facing us, and the need for increased and sustained congressional oversight and management attention.

MEDICARE

With annual payments of about \$200 billion, Medicare is one of the fastest growing major social programs in the Federal budget and is projected to almost double its size in the next 10 years alone. With responsibility for financing health care delivered by hundreds of thousands of providers on behalf of tens of millions of beneficiaries, Medicare is inherently vulnerable to fraud, waste, and abuse. The program has proven to be a perpetually attractive target for exploitation, requiring constant vigilance and increasingly sophisticated approaches to protect the system from wrongdoing and abuse.

The Department of Health and Human Services (HHS) has begun to identify improper payments in its financial statements for the \$176 billion Medicare Fee-for-Service program. Spotlighting the program's payment of claims has led to a number of actions to help prevent improper payments. Between fiscal years 1996 and 1998, the estimated total of payments made in error in this program dropped from \$23.2 billion to \$12.6 billion. The reductions in erroneous payments were attributable largely to better claims documentation by providers rather than a reduction in improper billing practices. The HHS Inspector General's methodology was not designed to identify or measure the full extent of fraud and abuse in the Medicare program or to detect all fraudulent schemes such as kickbacks or false claims for services not provided.³

Problems with abuse partly stem from the program's oversight structure. The Health Care Financing Administration (HCFA) delegates the review of claims to its contractors, yet its oversight of these contractors does not provide assurance that claims are paid appropriately. HCFA's contractors have allowed Medicare to pay claims that should have been paid by other insurers and have engaged in other prohibited practices such as falsifying claims and reports to HCFA.

MEDICARE CONTRACTOR PROBLEMS

In 1998, a major Medicare contractor settled a claim for \$140 million and pled guilty to eight felony counts because it was alleged to have

- allowed Medicare claims payments that should have been paid by private insurance,
- destroyed Medicare claims that should have been submitted by another contractor,
- periodically disconnected the required toll-free phone lines used for beneficiary inquiries,
- automatically paid claims under \$50, without checking whether services were uncovered or unnecessary,
- rushed claims through its processing system, shutting off computer edits designed to screen claims, and
- deleted, instead of suspending for review, claims with incorrect claim numbers

HCFA has taken steps to address management problems, but they remain hampered by financial management and information systems weaknesses. Moreover, the agency is limited by statute from increasing competition among contractors to enhance performance. For instance, the agency cannot choose nonhealth insurance companies to process outpatient physician and other practitioners' claims and is constrained to using contractors nominated by providers to process inpatient hospital and other institutional provider claims.

Medicare has also proven to be vulnerable to fraud by career criminal and organized crime groups posing as health care providers.⁴ These groups created sham

³ Medicare: Methodology to Identify and Measure Improper Payments in the Medicare Program Does Not Include All Fraud (GAO/AIMD-00-69R, Feb. 4, 2000).

⁴ Health Care: Fraud Schemes Committed by Career Criminals and Organized Criminal Groups and Impact on Consumers and Legitimate Health Care Providers (GAO/OSI-00-1R, Oct. 5, 1999).

medical clinics or other entities or used the names of legitimate providers to bill for services not provided or not medically necessary.

MEDICARE FRAUD: "RENT-A-PATIENT" SCHEME

In two South Florida cases, recruiters organized thousands of beneficiaries from, among other places, retirement communities and drove them to area clinics for rote examinations and unnecessary testing and treatment. Recruiters received a fee that they shared with each beneficiary. Beneficiaries understood that they should go elsewhere if they needed a "real doctor." Several licensed physicians participated in the scheme, in which they signed medical records for services they neither performed nor supervised. The clinics then billed Medicare and Medicaid or private insurance for services either not necessary or not performed. In one of the two cases, the clinics filed over \$120 million in fraudulent Medicare claims and \$1.5 million in fraudulent Medicaid claims.

Besides managing the fee-for-service program, HCFA has been grappling with the challenge of implementing the new managed care program—Medicare+Choice. Although the new program is premised on providing expanded choice to consumers, HCFA cannot ensure that the information provided to beneficiaries is timely, accurate, complete, or comparable or that beneficiaries receive the benefits to which they are entitled. For instance, one plan provided a drug benefit substantially less generous than what the plan had originally agreed to furnish, denying about 130,000 Medicare beneficiaries part of the benefit that Medicare paid for under the contract.

Strengthening business practices, controls, and oversight can mitigate program risks. Numerous initiatives are underway that promise to make progress. For instance, the HHS Inspector General and other Federal and state agencies have banded together to fight fraud in five states in an effort called Operation Restore Trust. After the first year of operation, the effort yielded more than \$40 million in recoveries of payments for claims that were not allowed under Medicare rules, as well as convictions for fraud, imposition of civil monetary penalties, and the exclusion of providers from the program. Over the long term, techniques developed by Operation Restore Trust will be applied in all 50 states. Moreover, 1996 legislation provided HCFA with increased funding for program safeguard activities, such as pre- and post-review of medical claims and fraud investigation units. These activities historically return more than \$10 in savings for each dollar spent. Clearly more needs to be done, but HCFA's use of financial statements and performance targets shows how appropriate management attention can help in measuring the extent and addressing the causes of improper payments.

Related program design problems further complicate Medicare service delivery and make costs more difficult to control. The following are two illustrations.

- Medicare payments for medical equipment and supplies may not reflect market prices when providers' costs for some procedures, equipment, and supplies have declined over time due to competition and increased efficiency. For example, Medicare payments for such items as walkers, catheters, and glucose test strips are based on supplier charges allowed in 1986 and 1987; prices for these items have dropped significantly since that time. The agency also does not have an effective system to know the specific products it is paying for. HCFA requires suppliers to identify on Medicare claims HCFA billing codes—most of which cover a broad range of products of various types, qualities, and market prices—rather than the specific items billed. For example, one Medicare billing code is used for more than 200 different urological catheters, even though some of these catheters sell at a fraction of the price of others billed under the same code.⁵ We have recommended that HCFA require suppliers to identify specific items by including universal product numbers on claims forms.

- Efforts to control Medicare home health care spending need to be designed such that payment levels are adequate and that appropriate benefits are being provided. Between 1990 and 1997, Medicare spending for home health care rose at an annual rate of 25.2 percent, making it one of Medicare's fastest growing benefits. By 1997, home health care consumed about \$1 of every \$11 of Medicare outlays, or about \$17.8 billion. To begin to control spending, the Balanced Budget Act of 1997 mandated a prospective payment system (PPS), which will be implemented on October 1, 2000. The PPS will pay a fixed, predetermined rate for each 60-day episode of care. The rate will be varied by a case-mix adjustment method that aims to adequately pay for patients with high services needs, yet not overpay for others with lower needs. Designing this mechanism requires detailed information, some of which

⁵ Medicare: Need to Overhaul Costly Payment System for Medical Equipment and Supplies (GAO/HEHS-98-102, May 12, 1998).

is not yet available, about services and beneficiary characteristics. Currently, there are large unexplained variations in patients' needs and services provided. Until necessary information on home health standards is available and the large variations in home health use are better understood, placing limits on the profits that agencies can earn under the new PPS will prevent Medicare from paying excessively for services delivered to beneficiaries. If the PPS rate is set too high relative to the actual cost of providing services, a profit limit would prevent a windfall from occurring for some home health agencies.⁶

SUPPLEMENTAL SECURITY INCOME

Supplemental Security Income (SSI) is the largest cash assistance program for the poor. In 1998, about 6.5 million SSI recipients received more than \$29 billion in benefits. Concern about the SSI program's vulnerability to fraud, waste, abuse, and mismanagement has increased congressional interest in ensuring that the SSI program focuses on individuals who have limited resources with which to meet their needs and that, to the extent possible, individuals rely on their own resources before turning to the SSI program for support.

Since its inception in 1974, the SSI program has been fraught with problems. These enduring management challenges—including program abuses and mismanagement, increasing SSI overpayments, and an inability to recover outstanding debt—continue. In fiscal year 1998 current and former recipients owed the Social Security Administration (SSA) more than \$3.3 billion—including over \$1 billion in newly detected overpayments for that year. Prior experience suggests that SSA is likely to recover about 15 percent of all outstanding overpayments. As we reported in prior work, SSI represents less than 8 percent of SSA's program expenditures but 37 percent of the calls to the fraud hotline and 24 percent of fraud convictions.

SSI FRAUD AND ABUSE PROBLEMS

- SSA has estimated that overpayments to recipients in nursing homes may exceed \$100 million per year.
- In 1998, we reported that about \$648 million in SSI overpayments occurred because clients did not disclose their earnings or financial account information.
- In 1996 SSI erroneously paid \$5 million to 3,000 current and former prisoners in 13 county and local jails because the incarceration was not reported to SSA.
- Between 1990 and 1994, about 3,500 SSI recipients admitted transferring ownership of resources such as cars, cash, houses, and land valued at an estimated \$74 million in order to qualify for benefits.
- Medical providers suspected of defrauding health insurance companies, Medicare, or Medicaid furnished a portion of the supporting medical evidence for 6 percent of 208,000 SSI disabled recipients in six states that we examined.

SSA has taken steps to improve the financial integrity of the SSI system. For instance, to identify illegal use of benefits by prisoners, incentive payments have been provided to correctional institutions for information on inmate benefits. In December 1999, the Foster Care Independence Act of 1999 was enacted and now provides SSA with several additional tools to improve program performance and integrity. These tools include the authority to obtain applicant income and resource information from financial institutions, access state databases for essential eligibility information, impose a period of ineligibility for applicants who transfer assets in order to qualify for SSI benefits, and use credit bureaus, private collection agencies, interest levies, and other means to recover delinquent debt. The act's provisions respond to many of our prior recommendations.

To a large extent, many of the problems facing the SSI program are the result of more than 20 years of inattention to payment controls. Although many of the changes enacted by the Congress or implemented internally by SSA should result in improvements, additional changes will be necessary to reduce the vulnerability of the program to waste, fraud, abuse, and mismanagement. Much of the problem has its source in an organizational culture that treats the SSI welfare program much the same way as its "earned benefit" programs, disability insurance and old age and survivors insurance. As a result, program staff have focused more on quickly processing claims than on controlling program expenditures and verifying eligibility. For instance, the agency's work credit measurement system rewards cases processed, not verification of eligibility and attention to fraud and abuse. Continued congressional oversight and top management commitment will be necessary to en-

⁶Medicare: Better Information Can Help Insure that Refinements to BBA Reforms Lead to Appropriate Payments (GAO/T-HEHS-00-14, Oct. 1, 1999).

sure that the agency diligently implements the new tools provided for in the Foster Care Independence Act of 1999. The agency has been proven reluctant to use some tools provided by the Congress in the past; for example, they received authority to do tax refund offsets in 1984 to recover overpayments but just started using it in 1998.

SSA should also continue to work with the Congress in addressing other vulnerable areas not directly addressed in the legislation. For example, SSA should move forward in developing options for addressing complex SSI living arrangement and in-kind support and maintenance policies, which our prior work has found to be a major source of SSI overpayments. Consistent with our recent report recommendation, SSA should also intensify its efforts to identify and track suspicious medical providers and other middlemen who abuse the SSI program. This information could help SSA identify claims that should receive increased scrutiny and better target its investigations of current beneficiaries to determine if they should be removed from the program.

OTHER IMPROPER PAYMENTS

Mr. Chairman, many other Federal programs in addition to Medicare and SSI are vulnerable to improper payments. I would like to highlight for you today a recent report we issued which addresses a number of specific programmatic weaknesses brought to light in our high-risk series and in agency financial statement audits.⁷ We noted that fiscal year 1998 financial statement reports from nine agencies reported estimated improper payments of \$19.1 billion—including \$14.9 billion in improperly paid expenses and an additional \$4.2 billion of receivables that these agencies expect to collect. These estimates related to 17 Federal programs that expended \$870 billion. The programs and related improper payment estimates include the following.

- Medicare Fee-for-Service (\$12.6 billion),
- Supplemental Security Income (\$1.6 billion),
- Food Stamps (\$1.4 billion),
- Old Age and Survivors Insurance (\$1.2 billion),
- Disability Insurance (\$941 million),
- Housing subsidies (\$857 million), and
- Veterans Benefits, Unemployment Insurance, and others (\$514 million).

GAO and agency inspectors general have identified many instances of fraud and internal control deficiencies which can lead to improper payments among these and other programs. Improper payments can arise from erroneous payments to beneficiaries as well as fraudulent or abusive practices by providers of services.

IMPROPER PAYMENT PROBLEMS

HUD assisted housing—A minister conspired with a real estate agent to defraud Federal housing officials. The minister made false statements in applying for a \$5.4 million HUD-insured mortgage for Bethel Village, a failed project of a religious affiliation to build an assisted living retirement development. The false statements included a letter, with the forged signature of the affiliation general secretary, that was sent to Federal housing officials guaranteeing \$750,000 in conventional funding for the project in order to obtain FHA mortgage insurance for the loan. (Source: Department of Housing and Urban Development, Office of Inspector General Semiannual Report to the Congress, Apr. 1, 1999-Sept. 30, 1999)

Food Stamps—147 out of 230 statistically selected Food Stamp participants whose Social Security numbers appeared in more than one state received food stamp benefits in more than one state simultaneously. This resulted in food stamp overissuances of \$43,000 for this group. In another case, from 1993 through 1998, a Cleveland, Ohio, grocer organized the illegal redemption of \$8.6 million in food stamps for himself and other Cleveland area grocers. (Source: U.S. Department of Agriculture, Office of Inspector General Semiannual Report to the Congress, Apr. 1, 1999-Sept. 30, 1999)

Veterans benefits—The spouse of a veteran, who had been collecting disability benefits for injuries sustained during his military service, failed to report her husband's death in 1983. VA benefits continued to be sent in the husband's name for more than 15 years. The widow converted more than \$243,000 of her deceased husband's benefit payments for her own use. VA computer records discovered this case

⁷Financial Management: Increased Attention Needed to Prevent Billions in Improper Payments (GAO/AIMD-00-10, Oct. 1999).

eventually. (Source: Department of Veterans Affairs, Office of the Inspector General, Semiannual Report to the Congress, Apr. 1, 1999-Sept. 30, 1999)

Social security benefits—A husband and wife embezzled Social Security benefits intended for the wife's deceased parents whose deaths were not reported to the Social Security Administration. Benefits of \$100,357 continued to be paid into the deceased couple's bank account. After their deaths, the daughter and her husband assumed the identities of the deceased parents and continued to access the funds for their own uses. (Source: Social Security Administration, Office of the Inspector General, Report to the Congress Oct. 1, 1998-Sept. 30, 1999, as incorporated in the Social Security Accountability Report for Fiscal Year 1999)

While financial statement disclosures draw attention to the need to address this problem, the amount of improper payments is greater than that disclosed thus far in agency financial statements. Audit reports from GAO and agency inspectors general have identified other agencies that have made improper payments but did not include estimates in their financial statements. For the Earned Income Tax Credit (EITC) program, in fiscal year 1998 when IRS examined a subset of returns with suspected EITC errors, it found that over two-thirds were invalid. This subset was not generalizable to all EITC claimants and IRS' financial statements did not contain any estimate of EITC error rates for the universe of returns claiming the credit.

In some cases, information is insufficient to provide systematic estimates of improper payments for other important programs. For instance, HHS has not estimated improper payments for the Medicaid program, which had \$108 billion in Federal outlays for fiscal year 1999. However, in recent work, we have concluded that the size and structure of this program makes it inherently vulnerable to exploitation. As a third-party payer, Medicaid reimburses for services provided by others and cannot, as a practical matter, police each claim for reimbursement. The program relies on providers, some of whom have incentives to exploit third-party payers like Medicaid, and program administrators, who are sometimes reluctant to impose controls perceived as burdensome for fear of discouraging provider participation. Common Medicaid fraud and abuse schemes fall into three broad groups: improper billing practices, misrepresentations of professional qualifications, and improper business practices such as kickbacks, self-referrals, or collusion.

MEDICAID FRAUD AND ABUSE PROBLEMS

Billing Fraud—A psychiatrist operated a "psychotherapy mill" where parents were enticed to enroll their children in "free" enrichment programs such as after-school tutoring, field trips, and supervised recreation in exchange for their children's Medicaid numbers. The psychiatrist then billed Medicaid for services not provided. In concert with another doctor, Medicaid was fraudulently charged \$421,000. The defendants pled guilty, paid fines and restitution, and received probation. (Source: Georgia State Health Care Fraud Control Unit)

Misrepresentation—A woman who never attended, graduated, or received a degree from a nursing school, presented a false nursing license to several nursing homes that employed her for at least 5 years. Her substandard care prompted an investigation, which led to her conviction of felony Medicaid fraud and other charges. She was sentenced to probation and either restitution or community service. (Source: Ohio Attorney General's Health Care Fraud Section)

Business practices fraud—Claims submitted by two businessmen netted \$10 million in excess Medicaid payments related to phony contracts with nursing homes to a shell company. They were both imprisoned and fined, and the pair agreed to restitution of \$6 million to the state Medicaid program. (Source: Georgia State Health Care Fraud Control Unit)

Illicit diversion of Medicaid covered prescription drugs has proven to be a chronic problem. Such diversion can involve pharmacists who routinely add drugs to legitimate prescriptions and keep the extra for sale to others; individuals who provide recipients with abusable drugs in exchange for subsequent illicit use of their Medicaid recipient numbers; and clinics that provide inappropriate prescriptions to Medicaid recipients who trade them for cash or merchandise or have them filled and then sell the drugs themselves on the street. The Congress could encourage HHS to increase its efforts as a partner with states to ensure that states' efforts to prevent and detect fraud in the Medicaid program are as effective as possible.⁸

⁸Medicaid: Federal and State Leadership Needed to Control Fraud and Abuse (GAO/T-HEHS-00-30, Nov. 9, 1999).

MEDICAID PRESCRIPTION DRUG FRAUD PROBLEMS

A criminal ring that included a doctor and others bilked the New Jersey Medicaid program out of hundreds of thousands of dollars. One scheme involved (1) doctors who wrote bogus prescriptions to Medicaid recipients in exchange for cash payments, (2) other recipients who served as the drug “buyers,” purchasing drugs using their own or false Medicaid cards and then selling them back to the ring, and (3) “runners” who brought the pills to a stash house for “packagers” who boxed the pills for resale to pharmacists in New York and New Jersey. The pharmacists would then use the repackaged pills to restock inventory. Sales of the drugs in New York yielded the ring \$30,000 or more in cash on a single trip. This case was the first health care fraud case prosecuted under New Jersey’s racketeering statute—one of a number of steps the state has taken to prevent fraud against Medicaid, Medicare, and private insurance.

With billions of dollars at risk, agencies need to continually and closely safeguard resources entrusted to them and assign a high priority to reducing improper payments. The incidence of improper payments can be reduced by strengthening business practices and developing targets or goals for mitigating the problem. A first step for some agencies involves the development of reliable estimates and reporting of the nature and extent of improper payments. Without this fundamental knowledge, agencies cannot be fully informed about their magnitude or trends, nor can they systematically pinpoint or target mitigation strategies. We noted in this report that it was through the discipline of annual audited financial statements and the development of performance goals—key components of the management reforms prompted by the Chief Financial Officers Act and the Government Performance and Results Act—that some agencies are taking steps to mitigate the risk of improper payments.

HUD PROGRAMS

In 1994, we designated HUD programs as a high-risk area because our work, and that of others, such as the HUD Inspector General, had identified four serious, long-standing, departmentwide management problems that, taken together, placed the integrity and accountability of HUD’s programs at high risk. These deficiencies included weak internal controls, an ineffective organizational structure, an insufficient mix of staff with the proper skills, and inadequate information and financial management systems. We concluded that, while HUD had efforts underway to address the numerous and severe problems impacting program management, billions of dollars across most of the agency’s programs were at risk.

Since 1995, we have reported that HUD has taken a number of actions to address its management deficiencies and has made credible progress toward improving its management. For example, the department improved its financial reporting to the extent that its Inspector General was able to provide qualified opinions on its financial statements for fiscal years 1996 and 1997 and an unqualified opinion for fiscal year 1998. In 1999, we noted that HUD’s Secretary and leadership team have given top priority to addressing the department’s management deficiencies. A major contributor to HUD’s progress was the June 1997 2020 Management Reform Plan, which called for reducing the number of programs, retraining staff, reorganizing the field offices, consolidating processes and functions into specialized centers, and modernizing and integrating information and financial management systems. However, in 1999 we also noted that internal control weaknesses—such as inadequate monitoring of contractors, developers, and other agents implementing HUD programs—and problems with information and financial management systems—such as inaccurate and untimely data—persisted. And, we reported it was too soon to tell whether HUD’s reforms to address organizational and staff problems would resolve the major deficiencies that others and we had identified.

Since then, we have undertaken a number of assignments to examine HUD’s efforts to improve its programs. For example, we have reported that HUD is likely to spend millions of dollars, miss milestones, and still not meet its objective of developing and fully deploying an integrated financial management system because it had not yet finalized detailed project plans or cost and schedule estimates for this effort. Also, both our office and HUD’s Office of the Inspector General have reported weaknesses in HUD’s oversight of its single-family inventory, which are properties acquired by HUD when borrowers default on single-family mortgages insured by HUD. In 1998, we reported that HUD did not have adequate systems in place to

oversee contractors who were responsible for managing its inventory of properties.⁹ Our physical inspection of selected properties identified serious problems including vandalism, maintenance problems, and safety hazards that may have decreased marketability, increased HUD's holding costs and, in some cases, threatened the health and safety of neighbors and potential buyers.

HUD's inventory of properties grew from about 39,000 in 1998 to about 50,000 properties in 1999. In 1999, HUD implemented a new approach to managing its acquired properties, under which contractors assumed full responsibility for the inventory. HUD awarded contracts to these contractors totaling \$927 million over 5 years and divided the country into 16 contract areas. One contractor, InTown Management Group, received 7 of the 16 contracts covering 28 states and comprising about 11,000 homes—in other words, almost 40 percent of the total workload.

Because InTown failed to adequately maintain properties or make them available for sale, HUD was forced to terminate all seven of InTown's contracts before the end of 1999. InTown filed for bankruptcy, while owing money to many of its subcontractors and these subcontractors now have filed liens against properties that InTown was responsible for managing and marketing. According to an official in HUD's Single-Family Housing Office, HUD has decided to pay off some of the liens. HUD also has awarded contracts to dispose of properties in 22 of the 28 states InTown had responsibility for. According to the Single-Family Housing Official, HUD issued a request for bids to obtain contractors for the remaining six states and expects to award these contracts by April 2000. We are presently reviewing the status of the contracts and HUD's inventory of acquired properties. We will report the results of our work this spring.

DOD MANAGEMENT

Six of our 26 high-risk areas relate to longstanding DOD management problems. The department's size, the complexity of its mission, and the far-flung breadth and scope of its operations present major management challenges in a number of areas.

Despite recent steps to improve financial management, DOD continues to face serious weaknesses. These weaknesses undermine DOD's ability to manage an estimated \$280 billion budget and \$1 trillion in assets. No major part of DOD is able to pass the test of an independent financial statement audit. These continuing financial management problems have real consequences for program management and resource allocation. For instance, DOD's records do not consistently reflect the number or location of its inventories and weapons systems. Auditors reported that DOD's records for F-4 engines and service craft were unreliable and that on-hand inventory quantities differed by 23 percent from inventory records at selected locations. These problems increase the risk that inventory managers may request funds for items that may already be on hand.

DOD cannot properly account for billions of dollars of basic transactions, leaving the agency vulnerable to the misuse of appropriated funds. DOD has not been able to reconcile its records with Treasury's records—with a \$9.6 billion difference at the end of fiscal year 1998. Auditors reported that the Air Force Depot Management Activity—a component of one of the department's working capital funds—may have obligated \$1.1 billion more than it had available as of September 30, 1998. Also at the end of fiscal year 1998, \$4.3 billion in expired budget authority was cancelled, another possible consequence of this inability to track obligations and expenditures.

Financial management weaknesses are reflected in DOD's procurement process where the agency spends more than \$100 billion a year contracting for goods and services. DOD continues to overpay contractors, although the full extent of overpayments is not known. However, we do know that from fiscal year 1994 through 1998, defense contractors returned about \$4.6 billion in overpayments, an average of about \$920 million a year. According to the Defense Finance and Accounting Services' Columbus Center, contractors returned about \$670 million in fiscal year 1999.

DOD CONTRACTING PROBLEMS

In a July 1999, study at 13 contractor locations, we found that these contractors took about a year, on average, before refunding overpayments of \$56.2 million. Four of the 13 contractors were retaining overpayments totaling about \$1.1 million, which they subsequently refunded due to our work. Under current law, however, there is no requirement for contractors who have been overpaid to notify the government of overpayments or return overpayments prior to the government issuing a written de-

⁹Single-Family Housing: Improvements Needed in HUD's Oversight of Property Management Contractors (GAO/RCED-98-65, Mar. 27, 1998).

mand for their return. In response to recommendations we made, DOD said it would amend the regulations and contract payment clauses to add a requirement that contractors notify the contracting officer when overpayments are discovered.

We have identified DOD's management of inventories (spare and repair parts, clothing, medical supplies, and other items to support the operating forces) as a high-risk area because levels of inventory were too high and management systems and procedures were ineffective. Ensuring the accuracy of inventory requirements, providing adequate visibility over operating materials and supplies, and reducing the vulnerability of in-transit inventory to waste, fraud and abuse remain areas of concern. The Congress has enacted legislation that requires DOD to implement best commercial practices in its acquisition and distribution of inventory items, and the Secretary of Defense has identified reengineered business practices as a key component of the Defense Reform Initiative. While these actions hold promise for the future, our recent work indicates that general areas of concern still exist.

DOD INVENTORY PROBLEMS

In November 1999, we reported that the Air Force did not always cancel purchases that exceeded current operating requirements. The Air Force canceled contracts for \$5.5 million of the \$162.4 million excess inventory that we reviewed—including such things as thermal insulation tiles for the B-2 aircraft and turbine nozzles for the F-110 engine—but it could have canceled more. For example, a requirement for a rotor blade used on the T-33 engine protected over 4 years of supply, thus preventing an additional 13,192 blades from being considered for cancellation.

Lastly, DOD's weapons systems acquisitions exhibit pervasive problems that lead to wasteful and ineffective systems. The agency spends over \$80 billion annually to research, develop, and acquire weapon systems. Although DOD has many acquisition reform initiatives in process, key weapon system problems persist arising from (1) questionable requirements and solutions that are not the most cost-effective; (2) unrealistic cost, schedule, and performance estimates; (3) questionable program affordability; and (4) the use of high-risk acquisition strategies. Weapon systems acquisitions remains a high-risk area, as indicated by some of the following examples from our work in the last year.

DOD WEAPONS ACQUISITIONS PROBLEMS

The Navy and Air Force plan to acquire 4,200 of the antiarmor Joint Standoff Weapon—a medium-range aircraft-delivered missile for attacking tanks and other armored vehicles—even though it is not effective against moving targets. The Air Force and Navy are implementing acquisition reform measures in the development of the Joint Air-to-Surface Standoff Missile that may not achieve their full cost and schedule benefits because of the services' historical practice of moving to the next stage of development prematurely.

The Army's Comanche Helicopter development program is being restructured for the fifth time in 10 years, due to uncertain and changing requirements and unattainable cost and schedule estimates. This latest restructured development plan still contains significant risks of further cost overruns, schedule delays, and degraded performance.

The Army procured 6,550 High Mobility Trailers that are not useable or suitable because it awarded a multiyear production contract without first demonstrating that the design would meet its requirements.

Although the number of armored targets (e.g., tanks) in current Defense plans is 80 percent less than in 1990, the military services plan to spend \$17 billion to acquire more new and improved antiarmor weapons. This would be in addition to the billions spent since the end of the Cold War to maintain and improve their large inventory of 40 different types of weapons for attacking tanks and other armored vehicles.

These are common examples that are the predictable consequences of the acquisition environment. The competition for funding when a program is launched encourages aspiring DOD program managers to include performance features that rely on immature technologies. In this environment, risks in the form of ambitious technology advancements and tight cost and schedule estimates are accepted as necessary for a successful program start. Problems or indications that the estimates are decaying do not help sustain programs in later years, and thus admission of them is implicitly discouraged. There are few rewards for discovering and recognizing potential problems early in program development. Acquisition reforms underway by DOD have the potential for improving weapon system outcomes and DOD's leadership is genuinely committed to making a difference in the status quo. However, lasting improvements in program outcomes will not come until the incentives that drive

the process are changed. Such changes will have to come in the form of the decisions made on individual programs.

STUDENT FINANCIAL AID

The Department of Education is responsible for collecting more than \$150 billion in outstanding student loans. Its data systems track about 93 million student loans and 15 million grants. In fiscal year 1998 more than 8.5 million students received more than \$48 billion in Federal student financial aid through programs administered by the department.

By their very nature these programs are vulnerable to waste, fraud, abuse, and mismanagement. Not only do they target a high-risk population, but also the programs have been designed to operate separately with different rules, processes, and data systems. Further adding to the vulnerability of these programs is the number of participants—not just millions of students and thousands of schools, but also thousands of lenders, guaranty agencies, third-party servicers, and contractors. The Federal Government bears most of the risk when students default on loans. Moreover, mismanagement by the Department of Education exacerbated the potential for abuses—weak gatekeeping allowed proprietary trade schools with poor educational programs and high student default rates to remain in the program.

STUDENT LOAN PROBLEMS

The Education Office of Inspector General reported that, between July 1, 1994, and December 31, 1996, 708 borrowers had loans totaling \$3.89 million discharged because guaranty agencies received a notice of their death. These borrowers were reported to have subsequently earned wages. For example, in 1997, 367 of these borrowers earned reported wages up to \$30,000, 191 borrowers between \$30,000 and \$50,000, and 150 borrowers more than \$50,000.

One borrower had student loans of \$8,517 forgiven because the guaranty agency determined, based on certification by the borrower's doctor, that he was totally and permanently disabled for work or school. There was no requirement for the agency to verify the borrower's disability or employment status with the state's employment agency. However, about 6 months later, the borrower received the first of four additional student loans totaling \$9565.

Between 1996 and 1999, an individual allegedly submitted 37 applications falsely claiming enrollment at four schools in Mexico, while he was on Federal supervised release. (He had previously been convicted of defrauding the education program of \$160,000 by falsely claiming attendance at a foreign medical school.) The 37 applications, which he allegedly submitted to four guaranty agencies, resulted in the disbursement of \$319,680. (Source: U.S. Department of Education, Office of Inspector General Semiannual Report to the Congress, No. 39, Apr. 1, 1999-Sept. 30, 1999)

Proprietary school owners mailed forged documents to loan servicing agencies in an effort to fraudulently reduce their school's student loan default rate to remain in the Federal Family Education Loan (FFEL) Program. The owners pleaded guilty to mail fraud, student financial aid fraud, money laundering and obstruction of justice. The 3-year scheme defrauded the Department of Education out of \$846,000 while the school avoided its eligibility from being terminated. (Source: U.S. Department of Education, Office of Inspector General Semiannual Report to Congress, No. 38, Oct. 1, 1998-Mar. 31, 1999)

Progress has been made. The department has made strides to improve its management of the program and has worked to effectively screen out schools with bad default records. Prior to the 1998 Higher Education Act amendments, students underreporting their income in applying for student aid had a better chance of never being caught. Over 300 students receiving Pell grants underreported their adjusted gross income by over \$100,000 each. Fortunately, the 1998 amendments directed Education and IRS to cooperate in verifying student income, but the effectiveness of this provision will be largely dependent on how well the two agencies work together. The default rate has declined from a high of 22.4 percent in fiscal year 1990 to 8.8 percent in fiscal year 1997. Nonetheless, in fiscal year 1997 the Federal Government paid out \$3.3 billion in defaulted loans.

The Department of Education lacks the financial information necessary to effectively budget for and manage its student aid programs and needs to work on improving the accuracy and completeness of its grant payments system. In addition, its lack of an integrated information management system means officials often lack accurate, complete, and timely data to manage and oversee aid programs.

SUPERFUND MANAGEMENT

GAO continues to have three concerns with agencies' management of the Superfund hazardous waste cleanup program. First, some agencies do not have a strategy for allocating resources according to risk. Since the Department of Energy (DOE) does not require facilities to compete for cleanup dollars, it may fund cleanups addressing a lower risk at one facility while a higher risk site at another facility goes unfunded. Another agency, the Bureau of Land Management (BLM), does not have a complete inventory of sites or a cleanup strategy in place and as a result potential hazards may expose the public to needless risks. For instance, BLM was not aware of one hazardous site until a child wandered onto the abandoned manufacturing site, came into contact with a contaminated rock, and fell ill.

Second, although the Environmental Protection Agency (EPA) has succeeded in getting responsible parties to pay for 70 percent of Superfund long-term cleanups, it has been less successful in recovering its full costs from parties when it conducts the cleanup. Figure 1 shows the problem.

FIGURE 1: EPA COULD LOSE THE CHANCE TO RECOVER BILLIONS IT HAS SPENT ON SUPERFUND (DOLLARS IN BILLIONS)



Source: GAO's presentation of data from EPA.

At the end of fiscal year 1998, EPA had agreements to recover only \$2.4 billion, about 22 percent, of about \$11 billion it had spent on the Superfund program.¹⁰ EPA's method for calculating indirect costs caused it to lose the chance to recover \$1.9 billion of the \$11 billion in settlement agreements already reached. This problem could lose the agency up to an additional \$1.3 billion in recoveries in cases under negotiation. EPA has updated the methodology for calculating and recovering indirect costs but has yet to implement it. The agency estimates that, with this new methodology, it could recover nearly half of the indirect costs that it currently excludes from settlements under negotiation.

Finally, EPA also needs to improve its contract management. The agency does not always negotiate the best contract price for the government. Although EPA is now using more independent estimating methodologies to help it negotiate contract prices than in the past, some of its regional staff still lacked the necessary cost estimating experience and training to help them negotiate best prices. In addition, EPA has more contract capacity in place than work available for the contractors. For example, EPA was reluctant to close out one contractor with high program support costs due to excess staff and facilities, even though it did not have sufficient cleanup work for the contractor. EPA has not effectively limited contractors' costs for program support, such as rent and managers' salaries. In April 1999, we reported that such costs ranged from 16 to 76 percent of total cleanup costs for new contracts, exceeding EPA's target of 11 percent. The agency is beginning to take additional steps to address this problem.

¹⁰EPA had spent another \$5 billion that it considers unrecoverable for reasons such as the lack of a financially viable party to cover the costs.

REDUCING AND RESOLVING RISK IN FEDERAL PROGRAMS

High-risk areas and improper payment problems reflect deeply rooted weaknesses in Federal financial and program management, as well as more fundamental tensions associated with conflicting statutory goals and complex program delivery systems and mechanisms. The government's financial systems are all too often unable to perform the most rudimentary bookkeeping for Federal entities, many of which are engaged in financial transactions whose magnitude, complexity, and risk exceeds those of large private companies. Weaknesses in underlying financial systems make agencies vulnerable by undermining their ability to safeguard assets, account for appropriated resources, or measure the costs of their activities. The agencies' inability to account for substantial liabilities, assets, net costs, or improper payments were among the factors that prevented us from being able to form an opinion on the U.S. government's consolidated financial statements for the 2 years that we have been performing this audit.¹¹ The lack of reliable financial information limits the capacity to even understand the dimensions of the risks the government faces—the first step in pinpointing strategies to mitigate problems. Agency efforts to implement the Chief Financial Officers (CFO) Act are prompting steady improvements, but, as shown in table 2, many Federal agencies were still unable to obtain a clean audit opinion on their financial statements in fiscal year 1998.

TABLE 2.—AUDIT OPINIONS FOR THE 24 CFO AGENCIES' FISCAL YEAR 1998 FINANCIAL STATEMENTS

Opinions	Agencies
Unqualified audit opinions: The financial statements are reliable in all material respects.	<ul style="list-style-type: none"> • Department of Housing and Urban Development • Department of the Interior • Department of Labor • Department of State • Environmental Protection Agency • Federal Emergency Management Agency • General Services Administration • National Aeronautics and Space Administration • National Science Foundation • Nuclear Regulatory Commission • Small Business Administration • Social Security Administration
Qualified audit opinions: Except for some item(s), which are mentioned in the auditor's report, the financial statements are reliable in all material respects.	<ul style="list-style-type: none"> • Department of Health and Human Services • Department of Energy • Department of the Treasury • Department of Veterans Affairs
Disclaimers: The auditor does not know if the financial statements are reliable in all material respects.	<ul style="list-style-type: none"> • Department of Agriculture • Department of Defense • Department of Education • Department of Justice • Department of Transportation • U.S. Agency for International Development
Other:	<ul style="list-style-type: none"> • Department of Commerce received an unqualified opinion on its balance sheet and a disclaimer on its other financial statements. • Office of Personnel Management's Retirement Program, Life Insurance Program, and Health Benefits Insurance Program received unqualified opinions; the Revolving Funds and the Salaries and Expenses Accounts received disclaimers.

Source: Individual agency reports on results of audits of fiscal year 1998 financial statements, as of October 1999.

While audited financial statements are essential to identify serious financial management problems and to ensure, and provide an annual public scorecard on accountability, an unqualified audit opinion is not an end in itself. The CFO Act is focused on providing accurate, timely, and relevant financial information needed for

¹¹ Financial Audit: 1998 Financial Report of the United States Government (GAO/AIMD-99-130, Mar. 31, 1999).

management decisionmaking and accountability, on a systematic basis, throughout the year. Efforts to obtain reliable year-end data that are not backed up by fundamental improvements in underlying financial management systems and operations that ensure the routine production of accurate, timely, and relevant data to support ongoing program management and accountability will not achieve the intended results of the CFO Act over the long-term.

For example, after several years of concerted effort by IRS and GAO, for fiscal year 1997 we were able to conclude for the first time that IRS' custodial financial statements, covering over \$1.6 trillion in tax revenue, were reliable. Prior to fiscal year 1997, weaknesses in IRS' internal controls and financial management systems prevented it from producing reliable year-end financial information. Our conclusion that the fiscal year 1997 statements were reliable was accomplished only after extensive use of ad hoc programming by IRS to extract data from its systems, followed by numerous adjustments to these data totaling tens of billions of dollars to produce final financial statements.

Serious and chronic financial management problems will continue to make agencies' programs and activities vulnerable to risk, waste, and mismanagement. Accordingly, we have added financial management at selected agencies to our high-risk list in recent years. Financial management at DOD and IRS were both added in 1995. The U.S. Forest Service and the Federal Aviation Administration (FAA) were added in 1999. These agencies face substantial challenges in producing reliable financial statements and reports due to serious deficiencies in financial systems and cost accounting. Although these agencies are making progress in addressing their financial management weaknesses, much remains to be done before full accountability can be achieved. Full accountability includes not only obtaining a clean audit opinion but also addressing internal control weaknesses which hamper their ability to keep track of their assets, liabilities, revenues, and expenses on an ongoing basis. For example, both Forest Service and FAA need to implement systems that are capable of properly recording, tracking, and depreciating property and equipment from acquisition to disposition.

Pervasive deficiencies in oversight, monitoring, and information systems by Federal agencies and by their agents in state and local governments and in the private sector also contribute to high-risk problems. In such areas as HUD's assisted housing programs and Education's student loans, local providers had primarily based eligibility on applicants' self-reported income, with little independent verification. These weaknesses in verifying the eligibility of beneficiaries have contributed to improper payments and are reinforced by fragmented organizational responsibilities and persistent human capital deficiencies. Organizational fragmentation, for instance, inhibits the systems integration necessary to prevent the needless duplicate entry of data in DOD's payment process that increases the probability of errors. Persistent staff skills mismatches have undermined HUD's capacity to effectively mitigate losses from foreclosures on its properties, manage troubled assets and prevent losses due to impending defaults on insured mortgages.

Resolving Federal management deficiencies is particularly important due to the complex delivery systems used in most Federal programs. The Federal Government often relies on a network of third parties—state and local governments, nonprofit agencies and businesses—to implement Federal goals. Third parties bring substantial advantages to the implementation of Federal initiatives by engaging local interests and resources. However, "third party government" poses challenges as well, since Federal programs rely on the integrity, skill, and support of independent agents with their own goals and constituencies. Transferring the responsibility for the delivery of services to third parties does not relieve Federal officials from being accountable for their performance. Many of our high-risk and improper payment areas are vulnerable due to the known challenges of Federal agency oversight of third parties that play a critical role in program implementation, including insurance contractors for Medicare; facilities management contractors at DOE; banks and state guaranty agencies for student loans; public housing authorities, mortgage lenders and contractors for HUD's housing programs; or states for food stamps and Medicaid.

Federal executive agencies are critical actors, but they operate within a broader statutory environment that can also play a role in promoting or mitigating risk. The design and incentives associated with Federal programs can often lay the groundwork for subsequent program vulnerability and delivery problems, while improvements can protect programs. For instance, the farm loan program reduced its delinquencies from 41 to 28 percent of its outstanding loan principal in 1997, due partly to earlier legislative changes prohibiting delinquent borrowers from obtaining further loans. However, recent legislation easing these reforms, along with deterioration in the farm economy, threaten to reverse this trend. In another area, high stu-

dent loan default rates were brought down when legislation provided for risk sharing by participating lending institutions and greater agency control over the certification of schools for participation in the program. Conflicting statutory goals can also complicate program administration; for example, programs emphasizing speed of service—such as mandates placed on IRS to process tax refunds within 45 days, or the urgency for the Federal Emergency Management Administration to provide disaster relief quickly—can confound the efforts of program administrators to reduce improper payments.

Mr. Chairman, the deep-seated nature of many of these problems does not mean they are immutable. In fact, we have noted substantial improvements in many of these areas. The point I want to make is that change is possible, but only with concerted and sustained attention of both executive agencies and often the Congress itself. Persistent improvements in information, systems, human capital, and program design are typically essential for progress to be made. Congressional oversight in particular is critical to stimulate and support the initiatives of agencies to address these problems.

The experience of the U.S. Customs Service (Customs) in overcoming its vulnerability to high risk is instructive. In 1991, we added Customs to our high-risk list due to major weaknesses in its management and organizational structure that diminished its ability to detect trade violations on imported cargo; collect applicable duties, taxes, and fees; control financial resources; and report on financial operations. Since then, Customs has made considerable progress in addressing its financial management weaknesses, receiving unqualified audit opinions for the past three fiscal years. Coupled with a major reorganization, Customs has also made major improvements in focusing on enforcement efforts and measuring noncompliance with trade laws, preventing or detecting any duplicate or excessive refunds, and collecting delinquent receivables. Sustained management commitment was essential for progress. It will be important for such management commitment and congressional oversight to continue in order to prevent these weaknesses from recurring. We will continue to monitor Customs' efforts.

IMPROVING THE ECONOMY AND EFFICIENCY OF FEDERAL ACTIVITIES

Addressing high-risk areas promises to diminish the vulnerability of Federal programs to fraud and abuse and reduce waste. In addition, other opportunities are present to increase the economy and efficiency of Federal programs and activities. Effective congressional oversight can improve performance accountability and financial integrity of existing programs by addressing the delivery strategies and structures used to implement Federal programs. Such an initiative can pursue opportunities for the consolidation or coordination of programs with similar objectives; the re-engineering and streamlining of Federal processes; the application of market-based models and prices to encourage the best use of Federal resources and the full collection of owed revenues and debts; and the integration of performance measurement with program management to identify more efficient and effective approaches to achieve Federal objectives.

The following examples from our work provide illustrations of programs and activities that could be considered for reform to address costly and inefficient delivery approaches, fragmented and duplicative organizational facilities and locations, or outmoded management structures.

- DOD's efforts at streamlining, consolidating, and possibly privatizing infrastructure activities should continue to be encouraged. For fiscal year 1998, DOD estimated that about \$147 billion, or 58 percent of its budget, was spent for infrastructure requirements. Recognizing that it must make better use of its scarce resources, DOD announced the Defense Reform Initiative (DRI) in November 1997. Through this program, DOD hoped to create a revolution in business affairs that would streamline and substantially improve the economy and efficiency of its business operations. A major thrust of the DRI was to reduce unneeded infrastructure, primarily through a number of initiatives designed to reduce the cost of DOD's operations and support activities. Included in these initiatives were (1) demolishing and disposing 80 million square feet of excess space at military facilities, (2) reducing the number of Defense Information System Agency major data processing centers from 16 to 6, (3) reducing the number of Defense Finance and Accounting Service operating locations from 19 to 11, (4) closing unneeded research, development, and test facilities, and (5) avoiding hundreds of millions of dollars in future capital expenditures by privatizing utility systems (electric, natural gas, water, and sewer) at military bases. The results of DOD's efforts in reducing infrastructure are mixed,

but continued progress on this initiative can help DOD save significant amounts of operations and support money.¹²

- The Department of State maintains a physical presence—embassies, consulates, and other offices in the capital and other cities—in over 160 countries. About 18,000 direct-hire employees—over 6,400 from State and the rest from at least 27 other Federal agencies—and over 35,000 locally hired and contract staff work overseas at a total of more than 250 diplomatic posts. It costs over \$200,000 annually to station an American overseas, which is about two times as much as for Washington-based staff. In November 1999, the Overseas Presence Advisory Panel, established by the Secretary of State to review how the United States carries out its overseas activities, concluded that there is no process in place to “rightsize” posts as missions change. Although the panel did not specify the amount of savings that could be achieved through streamlining posts, it expressed the belief that the savings would be substantial and recommended the formation of an interagency committee to review and restructure every overseas post. State has not said how it will respond to the panel’s recommendations. Security and diplomacy requirements are directly linked to the size of the overseas workforce, and the Congress should be involved in any significant restructuring.¹³

- Since 1982, many panels, commissions, and task forces, and several GAO studies have addressed how DOE could achieve operational efficiencies in its research and development facilities. Recommendations have included focusing unclear missions, aligning laboratory activities with DOE goals, consolidating facilities, and replacing cumbersome, inefficient management structures. In particular, with the end of the Cold War, DOE may no longer need to maintain three nuclear weapons laboratories. For example, Los Alamos officials have estimated that consolidating the nuclear weapons functions of the Lawrence Livermore facility into the Los Alamos Laboratory could save about \$200 million in annual operating costs. A DOE-chartered task force—the 1995 Task Force on Alternative Futures for the Department of Energy National Laboratories—reported that DOE’s entire laboratory system could be reduced productively by eliminating obsolete and redundant missions and support infrastructure.¹⁴ Moreover, substantial portions of the laboratory budgets are being spent on infrastructure.

- Duplication and overlap in Federal land management could be reduced and operations streamlined through a collaborative Federal land management strategy. The four major Federal land management agencies—the National Park Service, the Fish and Wildlife Service, and BLM within the Department of Interior, and the Forest Service within the U.S. Department of Agriculture (USDA)—have grown increasingly similar over time, while Federal land management missions have become more complex. Budgetary constraints and better understanding of natural ecosystems, whose boundaries are often not consistent with existing jurisdictional and administrative boundaries of the separate agencies, demand that the agencies find ways to refocus, combine, or eliminate certain functions, systems, programs, activities, and field locations. To improve the efficiency and effectiveness of Federal land management, the Congress might consider either reorganizing the current organizational structures or streamlining these structures by integrating and coordinating current functions and programs.¹⁵

- The Federal system to ensure the safety and quality of the nation’s food is inefficient and outdated. The current food safety system suffers from overlapping and duplicative inspections, poor coordination, and inefficient allocation of resources. For example within USDA, the Food Safety and Inspection Service (FSIS) is responsible for the safety of meat, poultry, and some eggs and egg products, while the Food and Drug Administration (FDA) is responsible for the safety of most other foods. FSIS, FDA, and 10 other Federal agencies administer over 35 different laws that oversee food safety. Given this environment, the Congress could consider consolidating Fed-

¹² Defense Reform Initiative: Organization, Status, and Challenges (GAO/NSIAD-99-87, Apr. 21, 1999).

¹³ State Department: Major Management Challenges and Program Risks (GAO/T-NSIAD/AIMD-99-99, Mar. 4, 1999) and Overseas Presence: Staffing at U.S. Diplomatic Posts (GAO/NSIAD-95-50FS, Dec. 28, 1994).

¹⁴ Department of Energy: Need to Address Longstanding Management Weaknesses (GAO/T-RCED-99-255, July 13, 1999) and Department of Energy: A Framework for Restructuring DOE and Its Missions (GAO/RCED-95-197, Aug. 21, 1995).

¹⁵ Federal Land Management: Streamlining and Reorganization Issues (GAO/T-RCED-96-209, June 27, 1996).

eral food safety agencies and activities under a single food safety inspection agency with a uniform set of food safety laws.¹⁶

- The USDA Farm Service Agency (FSA) should continue to consolidate its county office field structure by closing more of its small county offices. In response to the Agriculture Reorganization Act, FSA has closed over 370 county offices and reduced its county office staff by about 28 percent. However, FSA still has nearly 2,400 county offices, including 673 small county offices that have three or fewer permanent full-time employees. These smaller offices generally cannot take advantage of certain economies of scale. For example, USDA's workload data indicate that small county offices spend about 46 percent of their time on such fixed administrative activities as obtaining and managing office space and processing paperwork related to payroll. In comparison, larger county offices spend only 32 percent of their time on these administrative activities.¹⁷

- USDA's Rural Utilities Service (RUS) finances the construction, improvement, and repair of electrical, telecommunications, and water and waste disposal systems through direct loans and repayment guarantees on loans made by other lenders. Given demographic changes, the operating environment of today's utilities industry, and weaknesses in RUS loan management operations, the Congress could reconsider the role of RUS in the development of the utility infrastructure for the nation's rural areas. We have identified various steps RUS could take to increase the effectiveness and reduce the costs of its loan programs. From a financial standpoint, RUS has successfully operated the telecommunications loan program, but the agency has had, and continues to have, significant financial problems with the electricity loan program. For example, during fiscal years 1992 through July 31, 1997, RUS wrote off the debt of four electricity loan borrowers totaling more than \$1.5 billion. Since then, the agency has written off \$0.3 billion and is in the process of writing off an additional \$3.0 billion, and it is probable that the agency will continue to incur losses in the future.¹⁸

- Closing, consolidating or privatizing Coast Guard training and operating facilities could provide significant budgetary savings. In fiscal year 1996, we reported that the Coast Guard could save \$6 million by closing or consolidating over 20 small boat stations. Also in 1996, we recommended that the Coast Guard consider other alternatives—such as privatization—to operate its vessel traffic service centers, which cost about \$20 million in fiscal year 1999 to operate. In fiscal year 1995, we recommended that the Coast Guard close one of its large training centers in Petaluma, California, at a savings of \$9 million annually. The Coast Guard has faced, however, significant opposition to closing facilities.¹⁹

- The Commissioned Corps of the Public Health Service (PHS) was established in the late 1800's to provide medical care to sick and injured merchant seamen. As a result of temporary service with the armed forces during World Wars I and II, members of the Corps were authorized to assume military ranks and receive military-like compensation. Today, Corps officers continue to receive virtually the same pay and benefits as military officers, including retirement eligibility (at any age) after 20 years. However the functions of the Corps have become essentially civilian in nature, and, in fact, some civilian PHS employees carry out the same functions as Corps members. Further, the Corps has not been incorporated into the armed forces since 1952. Based on 1994 costs, when all of the components of personnel costs—including basic pay and salaries; special pay, allowances, and bonuses; retirement; health care; life insurance; and Corps members' tax advantages—were considered, PHS personnel costs could have been reduced by converting the Commissioned Corps to civilian status.²⁰

- The Department of Veterans Affairs (VA) owns 4,700 buildings and 18,000 acres of land, which it uses to operate 181 major health care delivery locations. VA spends about \$1 out of every \$4 of its \$18.4 billion budget to operate, maintain, and improve its delivery locations—in effect, the cost of its asset ownership. VA's delivery locations operate in 106 health care markets, and in 40 of these markets multiple VA facilities compete with each other to serve veterans—for example, 4 major VA

¹⁶Food Safety: U.S. Needs a Single Agency to Administer a Unified, Risk-Based Inspection System (GAO/T-RCED-99-256, Aug. 4, 1999).

¹⁷Farm Service Agency: Characteristics of Small County Offices (GAO/RCED-99-162, May 28, 1999).

¹⁸Rural Utilities Service: Opportunities to Operate Electricity and Telecommunications Loan Programs More Effectively (GAO/RCED-98-42, Jan. 21, 1998).

¹⁹Coast Guard: Review of Administrative and Support Functions (GAO/RCED-99-62R, Mar. 10, 1999) and Coast Guard: Challenges for Addressing Budget Constraints (GAO/RCED-97-110, May 14, 1997).

²⁰Federal Personnel: Issues on the Need for the Public Health Service's Commissioned Corps (GAO/GGD-96-55, May 7, 1996).

facilities are located in the Chicago market. However, all VA delivery locations project a declining veteran population base, and two-thirds expect declines greater than 33 percent in the next 20 years. Without major restructuring over the next several years, billions of dollars will be used to operate hundreds of unneeded VA buildings. For example, a VA study projected annual savings ranging from \$132 million to \$189 million by consolidating medical and administrative services at its major delivery locations in the Chicago area. VA needs to develop and implement realignment plans for all of its health care markets, and the Congress could consider a variety of options, such as greater reliance on community-based, integrated networks of VA and non-VA providers, to meet the health care needs of veterans in the most cost-effective manner.²¹

REASSESSING WHAT THE FEDERAL GOVERNMENT DOES

Addressing high-risk activities and pursuing opportunities to improve economy and efficiencies in government operations can yield significant improvements and cost savings and, hence, should be important targets for congressional oversight. However, it is also important to periodically examine whether current programs and activities remain relevant, appropriate and effective. Our work suggests that congressional oversight could usefully address three fundamental questions.

- Has a program succeeded, or persistently failed in accomplishing its intended objective(s)?
- Have underlying conditions that prompted Federal intervention changed such that original objectives are no longer valid?
- Have cost estimates risen significantly above those associated with the original objective(s), or have benefits fallen substantially below original expectations?

The following examples are illustrative of programs and activities that could be considered for reform, reduction, or termination because of fundamental changes affecting original objectives and purposes.

- DOD plans to develop and procure several aircraft, including the F/A-18E/F, the F-22, and the multiservice Joint Strike Fighter, to replace various types of tactical fighter and ground attack aircraft. As the nation proceeds to the next century with the prospect of a flat defense budget, DOD's plan to modernize its tactical aircraft fleet will be a significant issue confronting the Congress. DOD's planned investment in these aircraft, estimated by the Congressional Budget Office to exceed \$350 billion, is likely to be significantly greater than probable future budgets. Moreover, questions have been raised about the need for, and cost-benefit of, all these systems given likely threats. The traditional practices of approving all requested programs and then reducing procurement quantities within each program lowers acquisition costs but exacerbates the problem of aging equipment and associated operating and support costs. The Congress and DOD will need to carefully consider tactical aircraft investment options to ensure balance among bona fide national security needs based on realistic threat assessments, the desires of individual services, and what can be afforded given likely future budgets.²²

- The Army plans to invest over \$13 billion to develop and procure the Crusader self-propelled howitzer and its resupply vehicle to be used by the Army's rapidly deployable and forward-deployed forces. The Crusader program has experienced a number of problems that have delayed its development by 12 to 18 months, and a number of technical uncertainties remain. The Army has recently proposed changes to the Crusader artillery system to make it more affordable and relevant to future war plans. The new program reduces the planned procurement quantity, changes the armor, and cuts the system's weight to about 90 tons. Such changes, however, will likely reduce some of the Crusader's originally planned capabilities. Given the Crusader program's high acquisition costs and uncertain capabilities and requirements, other less costly alternatives—such as upgrading the Army's current Paladin system or procuring the German PzH 2000 self-propelled howitzer—could be investigated.²³

- The Army National Guard's combat structure, with 42 combat brigades, exceeds projected requirements for two major regional conflicts, according to war planners and DOD and Army studies. Although the National Guard has state missions in addition to its Federal role, a 1995 RAND study of the use of Guard forces for state

²¹ VA Health Care: Challenges Facing VA in Developing an Asset Realignment Process (GAO/T-HEHS-99-173, July 22, 1999).

²² Fiscal Year 2000 Budget: DOD's Procurement and RDT&E Programs (GAO/NSIAD-99-233R, Sept. 23, 1999).

²³ Army Armored Systems: Meeting Crusader Requirements Will Be a Technical Challenge (GAO/NSIAD-97-121, June 6, 1997).

missions concluded that, even in a peak year, such missions would not require a large portion of the Guard and should not be used as a basis for sizing the Guard's force. However, DOD has not yet addressed critical issues regarding the Guard's combat structure or eliminating any excess forces. As a result, the combat structure is left in place but has no valid war-fighting mission. Although the Army National Guard agreed to reduce its forces by 17,000 through fiscal year 2000, it did not agree to reduce overall force structure.²⁴

- The need for the Selective Service System could be reassessed. No one has been drafted in the United States since 1973 and the advent of an all-volunteer force. Since 1980, males between the ages of 18 and 26 have continued registering with the Selective Service System for a potential draft in the event a national emergency occurs. However, it would require congressional action to actually draft men into the military, and a return to a military draft seems unlikely, even under the current recruiting difficulties the military services are facing. One reason for this is that the recruiting shortfalls represent only a minute percentage of the over 13 million males of draft age and it would be very difficult to ensure a fair and equitable draft to cover such shortfalls. The likelihood of the United States engaging in a manpower-intensive conflict in the future is very remote, so alternative approaches to a draft could be devised to fill personnel needs. It has been estimated that it would take a little more than 1 year and funding equal to about 1 year's appropriation to bring the Selective Service System back from a "deep standby" status.²⁵

- The Uniformed Services University of the Health Sciences (USUHS) is a medical school operated by DOD. Those who propose closing the university assert that DOD's need for physicians could be met at a lower cost using physicians educated at civilian medical schools under the DOD scholarship program. USUHS is a more costly source of military physicians on a per graduate basis when DOD's and total Federal costs are considered. With DOD education and retention costs of about \$3.3 million over the course of a physician's career, the cost of a USUHS graduate is more than 2 times greater than the \$1.5 million cost for a DOD scholarship program graduate.²⁶

- The National Aeronautics and Space Administration (NASA) has estimated that the annual cost to operate the International Space Station (ISS) will average \$1.3 billion, or \$13 billion over a 10-year mission life. However, this estimate does not include risks associated with international partner commitments or other funding requirements, such as (1) costs associated with necessary upgrades due to component obsolescence, (2) end-of-mission costs to either extend or decommission the ISS, and (3) a variety of support costs (space shuttle flights, personnel, space communications, etc.) that are currently shown in other portions of NASA's budget.²⁷ Although assembly of the ISS is well under way, congressional oversight is vital to ensure that NASA's other priorities are not sacrificed in the agency's annual budget request to primarily fund ISS operations.

- DOE has lacked an investment strategy to assure that supercomputer acquisitions are fully justified and represent the best use of funds among competing priorities. From fiscal years 1994 through 1997, DOE spent about \$300 million to purchase 35 supercomputers and about \$526 million to operate them. Since fiscal year 1998, DOE has spent an estimated \$257 million to acquire additional supercomputers, most associated with the Strategic Computing Initiative. However, DOE used only about 59 percent of its available supercomputer capacity in fiscal year 1997 and was missing opportunities to share supercomputer resources. The largest supercomputers—those justified as needed to run very large programs across hundreds or even thousands of processors—were seriously underutilized. Less than 5 percent of the jobs run on those supercomputers used more than one-half of the supercomputers' available processors.²⁸

- The USDA Market Access Program (MAP) subsidizes the promotion of U.S. agricultural products in overseas markets. Despite changes made to the program between 1993 and 1998, its results remain uncertain. For example, our work has noted several unresolved questions, including whether subsidized promotions gen-

²⁴ Army National Guard: Planned Conversions Are a Positive Step, But Unvalidated Combat Forces Remain (GAO/NSIAD-97-55BR, Jan. 29, 1997).

²⁵ Selective Service: Cost and Implications of Two Alternatives to the Present System (GAO/NSIAD-97-225, Sept. 10, 1995).

²⁶ Military Physicians: DOD's Medical School and Scholarship Program (GAO/HEHS-95-244, Sept. 29, 1995).

²⁷ Space Station: Cost to Operate After Assembly is Uncertain (GAO/NSIAD-99-177, Aug. 6, 1999).

²⁸ Nuclear Weapons: DOE Needs to Improve Oversight of the \$5 Billion Strategic Computing Initiative (GAO/RCED-99-195, June 28, 1999) and Information Technology: Department of Energy Does Not Effectively Manage its Supercomputers (GAO/RCED-98-208, July 17, 1998).

erate positive net economic returns, increase exports that would not have occurred without the program, and supplement rather than supplant private sector spending.²⁹ Moreover, MAP promotions can have significant spinoff effects. For example, a 1996 study of U.S. apple exports to the United Kingdom and Singapore found that U.S. market share and export value increased in the United Kingdom, but that foreign competitors mainly benefited from MAP promotions in Singapore; Chilean and French apple producers experienced increases in export shares 3 to 10 times greater than U.S. producers. The Congress could reassess MAP and consider terminating or significantly reducing the program.

- The Coast Guard needs to develop a realistic estimate of needs based on the capabilities of its current fleet of ships and aircraft for its Deepwater Project, the largest acquisition project in the agency's history. The initial justification did not accurately or fully depict the need to replace or modernize its fleet of deepwater ships and aircraft. The agency's initial estimate that the project may cost \$9.8 billion, or about \$500 million annually over 20 years, would consume more than the agency now spends for all capital projects and leave little funding for other critical capital needs.³⁰

- To improve Amtrak's financial performance and potentially reduce Federal subsidies, the Congress must make fundamental choices between expectations for intercity passenger rail service and the Federal financial assistance that can be provided. These decisions involve determining the appropriate scope of Amtrak's route network and restructuring it accordingly, which could impact the need for financial assistance. Like other intercity passenger rail systems outside the United States, Amtrak receives substantial government support. Since 1971, the Federal Government has provided over \$23 billion in operating and capital assistance. Ridership in many areas is light: in 13 states, fewer than 100 passengers, on average, boarded an Amtrak train on a given day in 1997. A number of Amtrak's routes lost large sums of money in 1997; of the 40 Amtrak routes, 13 routes each lost over \$30 million and 14 each lost more than \$100 for every passenger. Overall in 1999, Amtrak lost \$907 million. In 1994, at the request of the administration and later at the direction of the Congress, Amtrak pledged to eliminate the need for Federal operating subsidies by the end of 2002. However, Amtrak has made relatively little progress in reducing its need for Federal operating subsidies; in fact, it must make nearly 4 times the progress in the coming 3 years (through 2002) than it has made over the previous 5 years. If Amtrak continues to require Federal operating subsidies after 2002, the Amtrak Reform and Accountability Act of 1997 provides for the Congress to consider either restructuring or liquidating the railroad.³¹

- Cargo preference laws require that certain government-owned or -financed cargo shipped internationally be carried on U.S.-flagged vessels. The laws were intended to guarantee a minimum amount of business for the U.S.-flagged vessels that are crewed by U.S. mariners, generally built in U.S. shipyards, and are encouraged to be maintained and repaired in U.S. shipyards. The effect of cargo preference laws has been mixed. Although the laws appear to have had a substantial impact on the U.S. merchant marine industry by providing an incentive for vessels to remain in the U.S. fleet, cargo preference laws have increased the government's transportation costs because U.S.-flagged vessels often charge higher rates to transport cargo than foreign-flagged vessels. Cargo preference laws increased Federal agencies' transportation costs by an estimated \$578 million per year in fiscal years 1989 through 1993 over the cost of using foreign-flagged vessels.³²

- The Medicare Incentive Payment program was developed to provide a bonus payment for Medicare services provided in areas identified as having a shortage of primary care physicians. About 60 percent of the payments, about \$65 million, was made to specialists; two-thirds of those payments—and many of the substantial bonus payments, such as \$69,000 to a dermatologist and \$57,000 to a neurosurgeon—were made to specialists in urban areas, rather than to primary care physicians in medically underserved areas. The bonus payments do not appear to have a significant impact on physician recruitment and retention, and recent beneficiary

²⁹ Agricultural Trade: Changes Made to Market Access Program, but Questions Remain on Economic Impact (GAO/NSIAD-99-38, Apr. 5, 1999).

³⁰ Coast Guard's Acquisition Management: Deepwater Project's Justification and Affordability Need to Be Addressed More Thoroughly (GAO/RCED-99-6, Oct. 26, 1998).

³¹ Intercity Passenger Rail: Amtrak Faces Challenges in Improving its Financial Condition (GAO/T-RCED-00-30, Oct. 28, 1999).

³² Maritime Industry: Cargo Preference Laws—Estimated Costs and Effects (GAO/RCED-95-34, Nov. 30, 1994).

survey information indicates that access problems arise for reasons other than the unavailability of physicians.³³

- The Government Printing Office (GPO), which receives over \$100 million in annual appropriations, effectively has a statutory monopoly over printing for the Federal Government.³⁴ GPO's monopoly-like role in providing printing services perpetuates inefficiency because it permits GPO to be insulated from market forces and does not provide incentives to improve operations and processes that will ensure quality services at competitive prices. Federal agencies could be given the authority to make their own printing policies, requiring GPO to compete with private sector printing service providers. If GPO is unable to provide quality service at competitive prices, the need for retaining a government printing office could then be reexamined.

REDEFINE WHO BENEFITS FROM FEDERAL GOVERNMENT PROGRAMS

The Congress originally defines the intended audience for any program or service based on a certain perception of eligibility and/or need. To better reflect changing conditions and target limited resources, these definitions should be periodically reviewed and revised. Our work has identified eligibility rules and subsidies to states, businesses and individuals that are no longer needed or that could be better targeted without changing the basic objectives of the program. As presently designed, a variety of grants, tax expenditures, loans and loan guarantees that provide subsidies to recipients who would have undertaken the activity without Federal subsidy and thus avoid bearing their fair share of risks and program finances. The following examples illustrate programs and activities that could be considered for reform, reduction, or termination because of changing conditions and perceptions of need.

- Many Federal grant programs with formula-based distributions of funds to state and local governments are not well targeted to jurisdictions with high programmatic needs but comparatively low funding capacity. As a result, it is not uncommon that program recipients in areas with greater wealth and relatively lower needs enjoy a higher level of funding than that which is available in harder pressed areas. For example, under the Community Development Block Grant (CDBG), Greenwich, Connecticut received five times more funding per person in poverty in 1995 than that provided to Camden, New Jersey, even though Greenwich, with per capita income six times greater than Camden, could more easily afford to fund its own community development needs. Better targeting of formula-based grant awards offers a strategy to bring down Federal outlays by concentrating reductions in wealthier communities with comparatively fewer needs and greater capacity to absorb cuts, while holding harmless harder pressed areas that are most vulnerable. For programs such as Medicaid, Foster Care, and Adoption Assistance, which base reimbursements on the per capita income of the state, the minimum Federal share could be reduced or the formula could be revised to better reflect relative need, geographic differences in the cost of services, and state tax bases. For other formula-based grant programs, such as Federal Aid Highways or the CDBG, the formula could be revised to reflect the differential fiscal capacities of states.³⁵

- The level and scope of the risks of the U.S. Export-Import Bank's (Eximbank) programs could be reduced by placing a ceiling on the maximum subsidy rate allowed, reducing or eliminating program availability in high-risk markets, and offering less than 100-percent risk protection. The Eximbank was created to facilitate exports of U.S. goods and services and is to absorb risks that the private sector is unwilling or unable to assume. Higher-risk markets constitute a relatively small share of the Eximbank's total financing commitments yet absorb a relatively large share of its subsidy costs. These changes would have only a slight effect on the overall level of U.S. exports supported with Eximbank financing. However, these options raise several trade and foreign policy issues that decisionmakers would need to address before making any changes in the Eximbank's programs.³⁶

- DOE and the private sector are involved in hundreds of cost-shared projects aimed at developing a broad spectrum of cost-effective, energy-efficiency technologies that protect the environment, support the nation's economic competitive-

³³ Physician Shortage Areas: Medicare Incentive Payment Not an Effective Approach to Improve Access (GAO/HEHS-99-36, Feb. 26, 1999).

³⁴ Government Printing: Legal and Regulatory Framework Is Outdated for New Technological Environment (GAO/NSIAD-94-157, Apr. 15, 1994).

³⁵ Formula Grants: Effects of Adjusted Population Counts on Federal Funding to States (GAO/HEHS-99-69, Feb. 26, 1999) and Federal Grants: Design Improvements Could Help Federal Resources Go Further (GAO/AIMD-97-7, Dec. 18, 1996).

³⁶ U.S. Export-Import Bank: Issues Raised by Recent Market Developments and Foreign Competition (GAO/T-NSIAD-99-23, Oct. 7, 1999).

ness, and promote the increased use of oil, gas, coal, nuclear, and renewable energy resources. Generally, DOE does not require repayment of its investment in technologies that are commercially successful. The potential for repayment can be significant. For example, we reported in 1996 that if only 50 percent of the funds planned for current projects were subject to repayment, and if about 15 percent of research and development funds result in commercialized technologies, then about \$400 million could be repaid to the Federal Government.³⁷

- Three Federal power marketing administration's (PMAs)—Southeastern, Southwestern, and Western—receive annual appropriations to cover operating and maintenance expenses and, if applicable, the capital investment in transmission assets. The fourth PMA, Bonneville Power Administration, does not receive annual appropriations. Federal law requires the PMAs to repay their appropriations as well as the power-related appropriations expended by the operating agencies that generate the Federal power. The PMAs are to set power rates at levels that will allow them to repay these costs. However for several reasons, the Federal Government currently is not recovering the full cost of its power-related activities from the beneficiaries of Federal power. For example, the Federal Government's financing of power-related activities results in a net cost because the interest rates on outstanding appropriated debt are lower than the rates Treasury incurs in providing the financing. Second, as we reported previously, the PMAs' had not been recovering the full costs of certain pension and other benefits for Federal employees involved in power-related activities. Currently, the PMAs are in varying stages of addressing this issue and DOE is considering changing departmental policy to ensure that these costs are recovered in the future. Third, the PMAs are able to sell power more cheaply than other providers because they market power generated almost exclusively at low-cost hydropower facilities, are not required to earn a profit, and do not fully recover the government's costs in their rates. For example, from 1990 through 1995, these three PMAs sold wholesale power to their preference customers at average rates from 40 to 50 percent below the rates nonfederal utilities charged. If the PMAs were authorized to charge market rates for power, some preference customers, who now purchase power from the PMAs at rates that are less than those available from other sources, would see their rates increase. However, slightly more than two-thirds of these preference customers would experience small or no rate increases—increases of one-half cent per kilowatt hour or less—if the PMAs charged market rates. Directing the PMAs to more fully recover power-related costs and requiring them to sell their power at market rates would better ensure the full recovery of the appropriated and other debt—which totaled about \$22 billion at the end of fiscal year 1997—that is recoverable through the PMAs' power sales, as well as lead to more efficient management of the taxpayers' assets.³⁸

- Federal water programs to promote efficient use of finite water resources for the nation's agricultural and rural water systems have developed inconsistencies that may cause the programs to work at cross-purposes. In the area of irrigation the multiplicity of programs and approaches has allowed for inconsistencies and potentially counterproductive outcomes. For example, under the Reclamation Reform Act of 1982, as amended, some farmers have reorganized large farming operations into multiple, smaller landholdings to be eligible to receive additional federally subsidized water. Due to the vague definition of the term "farm," the 960-acre limit established by the act has not stopped the flow of subsidized water to large holdings and the Federal Government is not collecting revenues to which it is entitled. Also, the use of federally subsidized water to produce federally subsidized crops results in the government paying double subsidies. The Department of the Interior estimated irrigation subsidies used to produce subsidized crops in the 17 western states to be about \$203 million in 1986; the Bureau of Reclamation placed the figure at \$830 million.³⁹

- The Mining Law of 1872 allows holders of economically minable claims on Federal lands to obtain all rights and interests to both the land and the hardrock minerals by patenting the claims for \$2.50 or \$5.00 an acre—amounts that fall well short of today's market value for such lands. Furthermore, miners do not pay royalties to the government on hardrock minerals they extract from Federal lands. For

³⁷ Energy Research: Opportunities Exist to Recover Federal Investment in Technology Development Projects (GAO/RCED-96-141, June 26, 1996).

³⁸ Federal Power: The Role of Power Marketing Administrations in a Restructured Electricity Industry (GAO/T-RCED/AIMD-99-229, June 24, 1999) and Power Marketing Administrations: Cost Recovery, Financing, and Comparison to Nonfederal Utilities (GAO/AIMD-96-145, Sept. 19, 1996).

³⁹ Rural Development: Patchwork of Federal Water and Sewer Programs is Difficult to Use (GAO/RCED-95-160BR, Apr. 13, 1995) and Water Subsidies: Basic Changes Needed to Avoid Abuse of the 960-Acre Limit (GAO/RCED-90-6, Oct. 12, 1989).

example, in 1990 hardrock minerals worth at least \$1.2 billion were extracted from Federal lands, while known and economically recoverable reserves of hardrock minerals remaining on Federal lands were estimated to be worth almost \$65 billion. The Congress could consider revising the law to require the payment of fair market value for a patent and to impose royalty payments on hardrock minerals extracted from Federal lands.⁴⁰

- The Federal Emergency Management Agency's (FEMA) Public Assistance Program helps pay state and local governments' costs of repairing and replacing eligible public facilities and equipment damaged by disasters. In a May 1996 report, we presented a number of options identified by FEMA's regional program officials that, if implemented, could reduce program costs. Among the options discussed was eliminating eligibility for private nonprofit organizations, many of which operate revenue-generating facilities such as utilities and hospitals, and publicly owned recreational facilities, which generate a portion of their operational revenue through user fees or admissions charges. Many of these types of facilities could have alternate sources of income sufficient to meet disaster-related costs.⁴¹

- Repetitive flood loss is one of the major factors contributing to the financial difficulties facing the National Flood Insurance Program. The Congress and FEMA could consider eliminating flood insurance and emphasizing mitigation for certain repeatedly flooded properties, removing what some argue is now an incentive to locate in harm's way. Approximately 43,000 buildings currently insured under the National Flood Insurance Program have been flooded on more than one occasion. These repetitive losses account for about 36 percent of all program claims historically (currently about \$200 million annually) even though repetitive-loss structures make up a very small portion of the total number of insured properties—at any one time between 1 to 2 percent. The cost to the program of these multiple-loss properties over the years has been about \$2 billion.⁴²

- We have reported in the past on this nation's practice of compensating veterans for medical conditions, such as diabetes, chronic obstructive pulmonary disease, arteriosclerotic heart disease, and multiple sclerosis, that were probably neither caused nor aggravated by military service.⁴³ In 1996, the Congressional Budget Office reported that about 230,000 veterans were receiving about \$1.1 billion in disability compensation payments annually for diseases neither caused nor aggravated by military service. Other foreign countries we reviewed require that a disability be closely related to the performance of military duty to qualify for disability benefits; no such link is required in the United States. The Congress could reconsider whether diseases neither caused nor aggravated by military service should be compensated as service-connected disabilities.

PURSuing EFFECTIVE OVERSIGHT: THE CHALLENGE AHEAD

Mr. Chairman, I am sure that this illustrative list of government performance and management problems is sobering. There is much to be done, but the task is not overwhelming. Given the demanding missions of our government and the sheer size and complexity of Federal operations, performance shortfalls should neither be surprising nor accepted. As my testimony today suggests, significant opportunities exist to curb fraud, waste, and abuse in a wide range of Federal activities and to update the priorities and program operations of the Federal Government in keeping with broader changes affecting our entire society and economy.

This is an opportune time to refocus congressional oversight. Not only are we free of the dominating concerns of the recent past—the Cold War and annual deficits—but we are about to begin to see the benefits of a wide-ranging reform agenda in the executive branch prompted by a series of laws—including the Government Performance and Results Act, the Chief Financial Officers Act, and the Clinger-Cohen Act—enacted by the Congress. The concerns of the Congress that led to the passage of those laws should now be directed toward a careful reconsideration of how the Congress will take advantage of and leverage the new information and perspectives coming from the executive branch management reforms.

⁴⁰Rural Development: Patchwork of Federal Water and Sewer Programs is Difficult to Use (GAO/RCED-95-160BR, Apr. 13, 1995) and Water Subsidies: Basic Changes Needed to Avoid Abuse of the 960-Acre Limit (GAO/RCED-90-6, Oct. 12, 1989).

⁴¹Disaster Assistance: Information on Federal Costs and Approaches for Reducing Them (GAO/T-RCED-98-139, Mar. 26, 1998) and Disaster Assistance: Improvements Needed in Determining Eligibility for Public Assistance (GAO/RCED-96-113, May 23, 1996).

⁴²Flood Insurance: Information on Financial Aspects of the National Flood Insurance Program (GAO/T-RCED-00-23, Oct. 27, 1999).

⁴³Disabled Veterans Programs: U.S. Eligibility and Benefit Types Compared to Five Other Countries (GAO/HRD-94-6, Nov. 24, 1993).

As agencies continue to make progress in implementing these financial and performance management reforms, we can expect further opportunities for congressional oversight to be revealed. The information they provide can assist in identifying weaknesses and illustrating programs and functions that are working well. Financial statements, for instance, are beginning to report information on improper payments, which is already helping to better target areas needing priority congressional and management attention. As more reliable financial information is developed and disclosed, new information will be forthcoming to inform resource allocation and oversight in other areas as well. For instance, audited information on the extent of Federal liabilities for environmental cleanup should help us better understand future cost pressures facing the budget and improve the cost effectiveness and targeting of our cleanup efforts. Similarly, the development of more reliable cost information should help us better manage these costs and make more informed trade-offs among competing programs and strategies to address Federal objectives.

The evolution of performance management should also assist oversight. The forthcoming publication of agency performance reports, due in March of 2000, comparing actual levels of performance against performance goals contained in agency plans, should help pinpoint both performance shortfalls and successes. These reports should also prompt inquiries to understand the factors responsible for performance outcomes, permitting a more systematic understanding of the role played by program design and management in influencing program results. The performance reports will also help us better understand strengths and weaknesses in agency performance information and data. Continued improvement in agency data should facilitate a deeper and broader assessment of the relative effectiveness of Federal strategies to achieve important goals.

In this context, I would note that the Administration has articulated an agenda in its fiscal year 2001 budget to improve financial and performance management across a wide range of Federal activities. Specifically, they have identified 24 priority management objectives dealing with many of the problems discussed in this statement. For instance, the Administration has included a goal addressing the improper payments problem and has promised to provide guidance to agencies on such issues as verifying eligibility criteria and estimating the extent of improper payment problems. Proposals are also advanced to strengthen the management capacities of HCFA and implement reforms at HUD, among other agencies. Continued top-level management attention to these issues is vital to making progress, as is congressional oversight of these initiatives.

As you know Mr. Chairman, oversight of Federal programs and activities can be a daunting challenge. While there may be some "low hanging fruit" in the examples I have just discussed, real improvements in performance and management will more likely call for a disciplined and determined approach. Many of the examples I have discussed come from longstanding weaknesses in management structures and processes and will likely require sustained attention over an extended period of time. Examining existing programs and operations entails taking a hard look at programs that often have become deeply engrained and carefully reconsidering the goals those programs were intended to address as well as how those goals are implemented. It involves sorting through the maze of Federal programs and activities where multiple agencies often operate many different programs to address often common or complimentary objectives. Addressing identified problems will call for hard choices; although offering distinct benefits, the choices will involve important stakes for many throughout our system.

Effective congressional oversight can be a means not only to identify where programs and activities should be terminated, but also where carefully selected investments by Federal agencies in human capital, technology, and financial and information management resources can yield important dividends in the form of longer term cost savings and improvements in performance. However, better information is needed to permit decisionmakers to sort through claims and to distinguish the infinite variety of "wants" from those investments that promise to effectively address critical "needs." Unfortunately, recent experiences ranging from information technology projects to major weapon systems illustrate that our return on such investments has been disappointing. Poorly conceived projects based on incomplete or inaccurate information and performance projections have led to projects with huge cost overruns and limited performance improvements. Although constructive change is occurring,⁴⁴ our work demonstrates the need to improve the basis for capital investments, in general, and information technology investments, in particular.

⁴⁴ Executive Guide: Leading Practices in Capital Decision-Making (GAO/AIMD-99-32, Dec. 1999).

I again commend you, Mr. Chairman, for holding these hearings and for reminding us all of the importance of continued diligence regarding the performance and management of government programs. Prudent stewardship of our nation's resources—whether in time of deficit or surplus—is essential not only to meet today's needs but also tomorrow's commitments and demands. Sustained congressional and executive agency attention to improving management systems and controls is vital to promoting proper stewardship of Federal resources and preventing risks of fraud, waste, and abuse that undermine the public's confidence in their government. Broadscale reexamination of Federal Government priorities, programs, and activities is also vital to ensure our capacity to meet current and emerging needs. We in GAO take very seriously our responsibility to assist you in promoting and ensuring accountability, integrity, and reliability throughout the government.

Chairman KASICH. Let me just ask initially, Mr. Walker, what percentage of your written testimony is covered in your oral testimony, would you say?

Mr. WALKER. I would say obviously the written is a lot more extensive. Maybe 15 percent.

Chairman KASICH. So we heard 15 percent, and we are all kind of worn out here after listening to this, I would say. [Laughter.]

Mr. WALKER. I am sorry, Mr. Chairman.

Chairman KASICH. And we only heard 15 percent. But I have been hearing this for 20 years. It is the same old stuff. It just makes my blood boil.

But, I understand that sometimes people say, well, if you look beneath the surface, you can find out that these things are really not so. I can remember defense contractors justifying \$75 apiece for nails.

There is always a way to explain anything. It just really gets to be—if it was my business and I had some employee that was—if I had a business and I couldn't add up my books, what do you think would happen? If I went to the bank and said I would like to borrow some money and I couldn't show them my books, I just plugged in numbers. I understand we are plugging in numbers at DOD, Agriculture, Education, Justice, Transportation, and AID. Correct?

Mr. WALKER. That is correct.

Chairman KASICH. We just plug in numbers because we can't make the numbers add up.

Mr. WALKER. Yes, intragovernmental transactions, transactions between agencies, there are real problems there.

Chairman KASICH. How do we get in a situation where we are buying these trailers in DOD?

Mr. WALKER. Quite frankly, Mr. Chairman, this is illustrative of a bigger problem.

Chairman KASICH. Well, let's talk about that problem. How are we buying a trailer that is not safe and that we don't need?

Mr. WALKER. Because DOD—

Chairman KASICH. Is there a Congressman up here that has it built in his district?

Mr. WALKER. I don't believe that is the issue, Mr. Chairman.

Chairman KASICH. OK.

Mr. WALKER. I mean, I think that DOD obviously has identified the fact that it has a mobility need and that it needed to do something to meet that need.

My understanding is that the problem that occurred here, Mr. Chairman, is they did not adequately define and test their speci-

fications before they awarded the contract and put it into production. So they defined what they wanted, but they didn't test the feasibility of it. And then by the time these things started rolling off the production line, they discovered they had some problems.

And, quite frankly, I think, as I said before, I can understand if we have to hurry up in the development of certain systems because of a credible external threat to our national security. However, we are in a very changed environment now. The nature of the threats that face us are fundamentally different than during the Cold War. And all too frequently DOD is cutting corners when there is no legitimate reason to do so. That results—that is waste. That is imprudent practice.

Now, we are doing work here on identifying commercial best practices for systems development, whether they be weapons or nondevelopment, which we are doing for the Congress, we are going to bring forward, and I think the Congress needs to seriously look at considering whether or not that DOD should be required to follow commercial best practices unless there is a clear, compelling national security threat to do otherwise.

Chairman KASICH. Now, my understanding is that little trailer there, it doesn't stay hitched. Is that correct?

Mr. WALKER. It either doesn't stay hitched, or if it does, it causes damage to the towing vehicle.

Chairman KASICH. OK. And they are asking for more of these. Is that right?

Mr. WALKER. About 18,000.

Chairman KASICH. More of them.

Mr. WALKER. That is correct, Mr. Chairman.

Chairman KASICH. Now, how can that be?

Mr. WALKER. Well, because they plan to—

Chairman KASICH. Who is in charge? I mean, seriously, how can that be?

Mr. WALKER. Well, they are confident they can fix it, Mr. Chairman, and my understanding is it is going to cost several hundred, maybe \$1,000 each. That frankly, unfortunately, is part of the mentality. It is part of the mentality. It is part of the culture. You know, let's get it while we can get it. Let's get it while we think we can get the funding, and we will worry about whether it works or we will worry about fixing it later.

That is not how you run a business. That is not how you run a Government.

Chairman KASICH. Where is it built? Do you know?

Mr. WALKER. Where is it built?

Chairman KASICH. Where is it built, yes.

Mr. WALKER. Oregon.

Chairman KASICH. Oregon.

Mr. WALKER. That is where the contractor is. Is that where the production facility is?

Mr. HINTON. It is not a contractor problem.

Mr. WALKER. It is not a contractor problem. It is a design specification problem, I believe. This is Butch Hinton who is head of our national security.

Mr. HINTON. Mr. Chairman, this is an Army management problem. When they started out with this program, they tried to adapt

the design to meet their needs without doing any testing. They only had procurement dollars available, and they went about their process by trying to make that work for them. And when they got into it and started testing, that is when all—as the Comptroller General has said, that is when the problems began to—

Chairman KASICH. It looks like a trailer. I mean, it doesn't look like it is a missile.

Mr. HINTON. It is a trailer. It just doesn't work for what they were trying to hook it up to do.

Chairman KASICH. So our answer is order 18,000 more of them.

Mr. HINTON. Well, we are going to keep an eye on that because—

Chairman KASICH. Oh, man, I feel better. [Laughter.]

Mr. HINTON. We are going to keep an eye on that. We asked the Army: Don't go forward until you can get this thing fixed.

Mr. SPRATT. Let me interrupt here, because it is our understanding the Army does not intend to order any more of these trailers. Have you not been notified as to that?

Mr. HINTON. I have not been notified to that, Mr. Spratt. In fact, when we concluded the work, they had plans for buying another 18,000, and that was at the end of—

Mr. SPRATT. Well, we were told that the remaining requirement is 18,412 additional units and that the Army will meet this requirement with a new trailer design, a new RFP.

Mr. HINTON. But I think, though, if they go through with a new trailer design, that is different than what we were told when we did our work. What we were told is that they were going to go back and modify—

Chairman KASICH. When were you told this?

Mr. HINTON. This would be in the September, October time frame of last calendar year.

Mr. SPRATT. Well, we have been told that the Army has established an integrated product team made up of representatives from the users, the safety and maintenance, program management, testing, procurement communities, the whole shebang, to see that this trailer meets both the subsystem requirements and the humvee trailer system requirements.

Now, who is the contractor for this?

Mr. WALKER. While he is looking for that, Mr. Spratt, our understanding was that they were not going to move forward acquiring any more until they got their problem fixed. Now, you may have more recent information, but I think—

Mr. SPRATT. They told us that they are going to go with a new design. They have already put together an integrated product team to develop that design. They are not ordering any more of this particular type of trailer.

Mr. WALKER. But even if that is true, Mr. Spratt—

Chairman KASICH. Let me tell you, I am just—I mean, what progress they have made on this. And I will bet you they are not ordering any more because we had investigators out there looking at them, and there was no way on God's green Earth that they were going to think they were going to order any more and get embarrassed on this. All right? So we don't have to talk about the trailer.

How about these? I mean, it goes on and on and on and on. Five changes in the Comanche helicopter, an unstable system. And so they decided somewhere between September and February to change their plans not to order 18,000 more. Why don't we give them a medal? Do we have any medals around here we can pass out to them?

The fact is that they were going to proceed on this, and they stopped. Good. I am going to write them a note this afternoon congratulating them. But the fact is—how many do they have of these?

Mr. HINTON. About 6,700, I believe.

Chairman KASICH. Maybe they stopped.

Mr. WALKER. Mr. Chairman, could I say one thing?

Chairman KASICH. Yes.

Mr. HINTON. They may well be doing what you said, Mr. Spratt. You may have more recent information than we do—

Mr. SPRATT. Do you know who the contractor is? I am just curious.

Mr. HINTON. Yes, sir. The original one was Electrospace Systems, Inc. in Richardson, Texas, which is now Raytheon E-Systems, Inc. It subcontracted to the Silver Eagle Manufacturing Company in Portland, Oregon.

Mr. WALKER. But I think the point that we were trying to make Mr. Spratt and Mr. Chairman, the basic way that the process works, this is an example. And, yes, they are obviously going to either fix this or they are going to go to new version because this one doesn't work.

But the problem is: How did we get to this point? And what systemic changes are going to be made to the process? No matter what team they have, what practices will the team employ in order to make sure that they are following commercial best practices so this doesn't happen again. And that is really the issue, because I am sure that they are not going to shoot themselves, repeat the same injury. I think we can probably reasonably agree to that. But they have got to fix the problem, and the problem is the system and the incentives and the accountability mechanisms in it.

Chairman KASICH. Let me ask you about—could you tell me anything about a charcoal grill at the Air Force Academy's Otis House?

Mr. WALKER. I think you brought that to our attention, Mr. Chairman. That is the \$14,000 grill?

Chairman KASICH. \$14,000 was spent to convert the charcoal grill at the Air Force Academy's Otis House to natural gas, according to the Air Force auditing agency. Another \$40,000 was designated for moving a bathroom wall at the house, the residence for the Commandant of Cadets, so that the adjoining bedroom's interior could be widened by one foot.

Is that kind of stuff still going on over there?

Mr. WALKER. Well, Mr. Chairman, we haven't done a review of that to be able to say whether it is still going on.

Chairman KASICH. Check it out for us, would you?

Let me ask you this question, seriously now. O&M, the number of dollars put into operation and maintenance readiness has gone from \$55,000 per troop to \$75,000 per troop. This is constant dol-

lars. You got me? \$55,000 per person to \$75,000 per person in constant dollars. That is for readiness.

Readiness indicators are down. Aircraft mission-capable rates are down about 10 percent. The Army recently declared two of its ten divisions not mission ready.

How can we put \$20,000 per troop in constant dollars into readiness but readiness indicators are going down? Can you explain that to me? Is that because we are not putting enough dollars in, or is that because we are not managing it properly?

Mr. HINTON. Mr. Chairman, we need to delve into the whole O&M issue here because a lot of the money which the Congress approves for a lot of the readiness issues moves out to fund other things such as real property maintenance needs and those type of things. That is one part of the answer. It doesn't really go to where some of it is needed because of other competing priorities.

Over time, we have seen a lot of movement of the O&M funds away from where the original request for those monies were needed and then they actually got spent. And that in turn drives that number up, and then it doesn't get to where some of the true readiness needs are.

I do also believe that OPTEMPO has a play in that issue, and it stretched some of the units to meet their priorities, and hence you have some of those units who are not capable of doing their missions.

Chairman KASICH. Mr. Spratt mentioned this issue of earmarks. You should know I have never had an earmark or an add-on in a defense bill or in any bill in the Congress in 18 years. Not one.

Mr. SPRATT. Mr. Chairman.

Chairman KASICH. Let me just ask this question about the—the gentleman will have his time in a second here, but I want to ask about the earmarks. I know there was a study done that indicated that the Congress had made a number of requests for weapons systems, you know, that the Pentagon didn't really want. Have you been able to review that lately, where are we on that? In other words, if we are driving these costs through the roof, have you been able to look at that, the number of weapons systems or whatever that the Pentagon did not want that we earmarked on both sides of the aisle that has created inefficiencies?

Mr. HINTON. We have not done a comprehensive review of that issue, Mr. Chairman. The only one of the programs that comes to my mind is where we looked at the C-130 aircraft issue in terms of the needs and the quantities there, and that is the only program we have looked at. But we haven't looked across DOD on that issue.

Mr. WALKER. Mr. Chairman, this is an issue that as recently as within the last week we have been talking about, as Mr. Spratt pointed out properly. In some cases, the problem is in the executive branch. Candidly, in some cases, the problem is in the legislative branch. In some cases, there are items that are appropriated for various reasons that aren't needed, and in some cases, there are restructuring efforts that DOD is desirous of undertaking that aren't undertaken. And that is part of the checks and balances, and, there are various considerations.

One example I would give you there is the base closure issue. It is a very emotional issue. We have been through that a couple of times already. DOD has said on more than one occasion that they would like to go through some more of those, that they think they are dedicating too much money maintaining unneeded infrastructure.

But there is a difference between that and making it a reality, and there are a lot of other considerations that have to be addressed.

Chairman KASICH. Let me get off of Defense for a second and talk about Education. I know that we passed in 1998 a data match requirement where we were to actually check the student applications and IRS data to make sure that people weren't getting loans, Pell grants, or whatever that they weren't entitled to. In 1998, they were to undertake a program to make sure that we verified people's legitimate needs.

Where does that program stand 2 years later?

Mr. WALKER. Well, first, Mr. Chairman, let me talk about what we are trying to do in this area in general, and then I am going to ask Vic Rezendes, who is the division head for that area, to address your specific question.

There is a data matching problem beyond education. There is a data matching problem in the entire Government. And one of the things that we are doing is not only continuing to do work on behalf of the Congress, we are actually pulling together some people at the GAO to try to help some progress get made on this throughout the Government in order to try to get some results here.

Vic.

Mr. REZENDES. Basically, the issue is one of IRS' comfortableness with opening up its records for data match, not only with Federal agencies but particularly on the Department of Education issue. Their primary concern is opening up this and giving this to private contractors and other third parties.

I believe the IRS position is they would prefer to see Congress authorize specific legislative authority for them to deal with this.

Mr. WALKER. So they are not making the progress because they would rather be mandated.

Mr. REZENDES. Right. They are still negotiating. But I think IRS' position is they prefer Congress to direct them to do this.

Chairman KASICH. I thought we directed them to do it.

Mr. REZENDES. Through the Education Act, but they are looking for a more generic fix in the statute for matches throughout the Federal Government.

Mr. WALKER. Mr. Chairman, the problem appears to be at the IRS rather than at the Department of Education. It is the IRS that is looking for some type of direction and some type of comfort.

Chairman KASICH. Why don't you get us some language so that we can move on this?

Mr. WALKER. We will follow up on that.

Chairman KASICH. In other words, 2 years later, Education says we—they are directed by the Congress to do a match, and the IRS says we aren't going to do a match. So 2 years later, there is no match going on. Is that it?

Mr. REZENDES. That is correct.

Chairman KASICH. Let me ask you about prescription drugs. Medicaid accounts for 80 percent of all Federal spending on prescription drugs. We don't know how much waste there is in this program—is that correct?—because we don't aggressively audit because it is a Federal and State program. Is that correct?

Mr. WALKER. We don't know the total amount.

Chairman KASICH. The State of New York reported that at least 10 percent of the State's total Medicaid spending for prescription drugs were losses. So 10 percent of all the money spent on prescription drugs in New York was lost. They don't know what happened to it, according to New York.

What can we learn as we move forward into a prescription drug program for Medicare from what we have learned from Medicaid, anything? Since we haven't audited it—

Mr. WALKER. I think there are a number of things that we have to keep in mind in conjunction with prescription drugs:

Number one, they are the fastest-growing component of health care cost.

Number two, there is a bona fide need to look at access to prescription drug coverage to the population, especially the Medicare population, but there is a difference between access to coverage and who pays for the coverage.

Number three, there is a possibility to engage in some group purchasing and then pass those savings along on a cost-neutral basis.

And, number four, if the Congress is going to do anything on prescription drugs, for example, in Medicare, it should target the financial assistance to those who truly need it.

But in addition to that, I think we need more transparency. We need more incentives with regard to health care in general and prescription drugs in particular, so that individuals are more sensitive to the cost and can identify possible abuse where drugs are being billed that haven't been received. Part of that is challenging when you are dealing with the seniors population, some of which could be well into their 80s and may not be in the best position to be able to make some of those judgments. But we have got to learn some of those lessons before we move forward.

Chairman KASICH. What you are saying with the Medicare system, this proliferation of payments—and I am going to try to move on and give time to Mr. Spratt, because we have got a long way to go today—is that you have a systemic problem. When 900 million claims are filed every year and I am not making the purchases myself and somebody else is involved, you have got a systemic problem when it comes to how you do health care.

Mr. WALKER. There is a systemic problem, and it is much bigger than Medicare, and Medicaid.

Chairman KASICH. Let me just ask a final question. First of all, we order a lot of things, and we pass a lot of things, and nothing happens in too many cases. How do we get on top of that to make sure that things actually happen? I suppose there is no substitute for the will of a member who just locks on and doesn't let go. And, secondly, if you were to be in a position of actually trying to force some of these things to happen, how would you systematically go about focusing on each of these areas so that either we can have

proper congressional oversight either to change things or to make sure that what we have already passed is going to be implemented?

Mr. WALKER. Well, first I think it is important for the accountability community, meaning the GAO, the inspectors general, and the others, to be able to coordinate their efforts to make sure that we are focusing on the areas where there is the greatest possibility for return, that we are not duplicating efforts.

Secondly, I think it is important that OMB play a major leadership role throughout the executive branch and spend more time on management. OMB spends a lot of time on budget. They are starting to spend more on management, but not nearly enough.

Thirdly, I think the Congress needs to reinvigorate oversight. I think the example of the Customs Service is a positive example of where the executive branch took it seriously, the Congress took it seriously, and we got it off the high-risk list. And we got it off the high-risk list in a couple of years.

So it is a matter of focus. It is a matter of efforts by both the legislative and executive branch as well as the accountability community.

Chairman KASICH. I wonder if you could send us a real good analysis of what Customs did. What did Customs put in place? They had to admit their problem. What were the steps that they took? And maybe we can learn from Customs and that can be helpful in terms of how these other governmental entities are able to improve.

Mr. Spratt.

Mr. SPRATT. Well, we gave them the money to buy a new computer system. I went up to the terminal in Newark to see how the Customs system tracked textile imports years ago, and they were so bereft of contemporary computer systems that they were literally using the computers that the import terminals themselves maintained. They put their software on the terminal's hardware just because it was better than anything the Government was providing. And we provided them the money, a substantial sum of money, for modernization and it is beginning to pay dividends.

Mr. WALKER. I think there are several issues here. You are pointing out an important point. It was leadership, it was focused, it was sustained commitment. But in some cases, in order to solve some of these problems, you may have to make some targeted investments—not in all but in some you may have to—in order to be able to generate the savings.

Mr. SPRATT. One of the investments you haven't mentioned is people, not just investing in people but the sleeper problem in the Federal Government, the thing you haven't discussed here today, is how do we attract our share of the best and brightest to work in the Federal Government. You can have systems; you can have precepts and rules and regulations. If you don't have bright people to run these systems, you are going to have problems like these.

Mr. WALKER. I really appreciate that. As you probably know, I have a strong, longstanding interest in the area of human capital, which is people.

The three biggest enablers to any enterprise, whether it be the private sector, the not-for-profit sector or Government, are people,

process, and technology. And people represent the most important element.

Mr. SPRATT. It comes way ahead.

Mr. WALKER. And the fact of the matter is I believe that on our next high-risk list, there are probably going to be two areas across Government that are going to be on that. One is the Government's emerging human capital challenge. It has a major problem in the area of people because the effects of downsizing. We need to have the right people with the right skills focusing on the right things for the future. We have got succession planning problems, et cetera.

In addition, we have got a contracting problem. We have got a lot of situations where a lot of functions in the executive branch have been outsourced to third parties, but we don't have the people with the skills to monitor and to manage cost and quality. So we are on autopilot, and we are subject to abuse. Those two areas are high risk, in my opinion. We haven't made the final judgment, but I believe in all likelihood they are going to be on there.

Mr. SPRATT. Just to shift the focus a little bit and leaven the atmosphere somewhat, aren't there some cases where we have made improvements? Let's take the Department of Education, for example. In the early 1990s, it is my understanding that the student loan default rate was running well over 22 percent, and today I believe, according to my information, it is 8.8 percent.

Do you have that information? Can you validate that? Is that correct?

Mr. WALKER. Mr. Chairman, Vic Rezendes—or Mr. Spratt. I am sorry.

Mr. REZENDES. That is exactly correct. In fact, they have a performance measure that they have included in their current plans that caps it at about 10 percent. Obviously, I think everybody would like to have the default rate at zero.

Mr. SPRATT. Sure.

Mr. REZENDES. But the reality is the target population we are providing loans to are people who basically find it difficult to find commercial loans to go to college.

Mr. SPRATT. And Secretary Riley has tried to implement, in lieu of these student loans and really just to have another measure, felt he could do it more efficiently, some direct loans, loans made directly by the Department as opposed to guaranteed loans.

Now, they tell us that the direct loans are saving money. Can you validate that?

Mr. WALKER. Mr. Chairman, we haven't done the work to be able to express an opinion on that one way or the other.

Mr. REZENDES. The IG may when she testifies later.

Mr. WALKER. The IG might be able to tell you something more, but we—

Mr. SPRATT. It has been a hard sell in Congress, but according to the Department of Education, it has been a successful program. They are actually making money. Where they lose money on student loans, they are making money on direct loans because the rate of interest they charge is higher than the Government's cost of money and the cost of administration.

Mr. WALKER. As I said, we haven't done the work on that, but I will follow up on one of your comments which I think is important. There has been progress in some of these areas, and I tried to acknowledge that, as well as in our statement. And I think it is important that not only we try to find out what is wrong with Government and the fact that we should have zero tolerance for fraud, waste, abuse, and mismanagement. It will never be zero. In the largest, most complex, most diverse entity on Earth, it will never be zero. But we should have zero tolerance. We have got to focus on what we can do to accelerate progress in these areas, and we have got to focus on dealing with the systemic problems, the things that may not be that sexy.

But, the taxpayer is going to get a lot bigger return on their investment if we make sure they got the right people, with the right technology, with the right performance standards, with the right systems—a big return on investment.

Mr. SPRATT. Well, I don't think any of us wants to leave the impression or should leave the impression that this is a totally bleak picture and that there is absolutely no response, no improvement, that this is a constant drumbeat of bad news and nobody ever does anything about it.

There are continuing problems and there will be bigger problems because the Government gets bigger and the dollars get bigger. Medicare is a good example. You said it would double in cost. But a couple of years ago, we began giving the Department of Health and Human Services more money to go into audit work, field investigations, and things like this. And HHS tells us that they have had significant, measurable results.

Based on a statistical sample, the IG at HHS estimates that Medicare's net overpayments for fiscal year 1998 totaled about \$12.6 billion nationwide. Now, that is still a huge amount. That is 7.1 percent of the total benefit payments. But in fiscal year 1996, the estimate of overpayments was \$23.2 billion, so the current estimate, based on the sample, is 45 percent less than it was 2 years ago, about \$10 or \$12 billion better than it was just a couple of years ago because they have begun to focus on it and we have begun to focus on it, too, and put some of our money where our mouth is.

Mr. WALKER. I think that is an example where progress has and can be made. For example, we worked with the IG and the Congress was focused on it as well. The Department was focused on it. But I think there is an important footnote.

You are correct. It has come down, and it has come down significantly. But most of that reduction has been in the providers providing better documentation for their billing. We haven't made nearly as much progress in improper payments due to lack of medical necessity, incorrect coding, and the coverage categories. But those are tougher to get to.

So, yes, we have made progress, but in some ways, we are getting to the tougher part of the challenge now.

Mr. SPRATT. Mr. Chairman, I don't want to jab at you, but just in the gist of saying that none of us who has been here any significant period of time is really pure, I seem to recall that Mr. Kasich wanted to buy more B-1B bombers in lieu of B-2 bombers, about

20 more, when the Air Force said we need to stop the program. Systems integration is a major problem. There was a system called the ALQ-161. You couldn't turn on the defensive systems and the offensive system at the same time. And I think some major part of it was built in your constituency.

That is not to criticize you because we all come here as advocates for what is happening in our own constituency, but it is to say that many of us at one time or another are part of the problem. And I am as guilty as anybody, so let me profess my lack of purity on the record.

Chairman KASICH. Well, let me just say this: I never have had an add-on, a highway project, the entire time that I have been in this Congress.

Mr. SPRATT. Yes.

Chairman KASICH. And the fact is back during the B-1 debate, the Air Force wanted more of those B-1s, and they didn't get them. And that was the end of it. But the fact is that if you look through the record of either highway projects or your add-ons in the Armed Services Committee, or whatever other thing, you can't find any that I have done. And that doesn't mean that people who have had these things are somehow wrong.

We are having a big debate right now, a Presidential campaign about the issue of pork. Pork is a matter of whether it is built in somebody else's district, not if it is built in your district. But the problem is when Members in depot caucuses or whatever, are working against the interests of the Pentagon and forcing them to buy things that they don't want. I have never engaged in that and—

Mr. SPRATT. You need a system where you can represent your own constituency, but the institution is strong enough so that if it is not for the good of the country, then you don't prevail.

Chairman KASICH. Right. And it is interesting, because of the B-2, we were going to order 132 and we ended up buying 20 of them. And so we saved I don't know how many billions and billions of dollars, and now it is kind of interesting that the B-1 is a pretty effective part of our force.

Mr. SPRATT. Let's be fair. The B-2 acquitted itself pretty nicely in Kosovo and the Bosnian war, too, the Yugoslavia war. That is a total aside, but I couldn't resist it. I am sorry.

Thank you, Mr. Chairman.

Chairman KASICH. Mr. Gutknecht is recognized.

Mr. GUTKNECHT. Thank you, Mr. Chairman. And I want to thank you for this hearing and Mr. Walker and his entire team for presenting to us today. To paraphrase I think what Patrick Henry said a long time ago, the price of accountability is eternal vigilance, and I hope that we will have more of these hearings.

If my arithmetic is correct—and I am doing this on the back of a napkin—we bought 6,700 of these trailers at a cost of roughly \$10,000 apiece. That is \$67 million that has been spent. Is that correct?

Mr. WALKER. Somewhat over, but you are close.

Mr. GUTKNECHT. I think the real question here is: Was anyone involved in this program demoted or lose their job?

Mr. WALKER. I can't say that. We could try to find out. But I will tell you this: I think history has shown that there is not enough accountability for these types of mistakes.

Mr. GUTKNECHT. I think that is the issue, and that is where I would hope that we would have an ongoing effort in this committee and maybe target certain areas and go through them as best we can to at least focus some attention on what is happening.

Now, I am not saying that people necessarily should be fired, but I will tell you this: I think in the private sector whoever was in charge of that project would at least be demoted, or there would be some kind of an action taken for people who would go ahead with something like this.

You list on your chart—and you did not really get to it. And I also serve on the Science Committee. I have been very interested in this whole upgrade of the FAA system.

Now, as best I can determine, we have wasted billions of dollars there in trying to come up with a whole new system, and I think most travelers would be shocked to realize that in most air traffic control centers, the air traffic controllers are still looking at screens that were built in the late 1950s.

Do you have any more information? Are we making any progress to finally get the FAA system upgraded? And, to the best of your knowledge, how much money has been spent in that effort?

Mr. WALKER. Let me touch on an overview and then ask Keith Fultz, who is head of that division, to address you.

IT is another area, when you are talking about development and acquisition practices, that is a major problem in trying to help do design specifications, in turning over too much responsibility to the contractor without having an adequate number of skilled people to be able to manage cost and quality. This is one example of that, and I would like Keith Fultz to address your question directly.

Mr. FULTZ. To the best of our knowledge, the costs to date for the air traffic control modernization program is approaching \$42 billion. In the late 1980s, the original estimate was somewhere in the \$8 to \$9 billion range.

Mr. GUTKNECHT. So the original estimate was \$9 billion, and we have already spent \$42 billion, and it still is not done.

Mr. FULTZ. We still have some major challenges that need to be addressed before the system is complete.

Mr. GUTKNECHT. Can I just switch to another quick topic? Because I know my time is limited. You also mentioned the IRS and receivables. You mentioned a number of things with the IRS, at least in the chronology of high-risk designations.

We have had some discussion here in the Congress—and some of us got beat up a bit last fall—about the earned income tax credit, but there is quite a bit of evidence, at least as far as I am told, that relates to—we all hate the word “fraud,” but apparently there is almost a business developing out there of encouraging people to misrepresent what they may be eligible for in the earned income tax credit.

Do you have any more information on that?

Mr. WALKER. My understanding is that, based on some work that we have done, there could be as high as about two-thirds, I believe, of questionable activity in conjunction with EITC.

Mr. GUTKNECHT. Could you put that in numbers? What is that ultimately costing us?

Mr. WALKER. Jeff Steinhoff can address that.

Mr. STEINHOFF. IRS focused on a sample of those returns they thought might be suspect—\$662 million worth of returns—and found that \$448 million were, in fact, invalid claims.

No one knows the full extent of this. It gets down to that we do have a voluntary compliance system. IRS does have a 45-day period to make a refund, and what you do not have are the detective controls up front. You have got back-end checking.

So there were a number of instances found of people coming across border towns, weren't even U.S. citizens, claiming the credit. Under this particular credit, you don't have to pay any taxes. You are just getting back money.

So, again, it is more of a pay-and-chase situation for the IRS. They will pay it out, and then they will have to come back and see if they can, in fact, recoup those monies.

Mr. WALKER. I think it is important to note, however, that the sample that they picked was not a valid sample.

Mr. STEINHOFF. Right, right.

Mr. WALKER. So, therefore, of the ones that they thought might have a problem, it turns out two-thirds of them did have a problem.

I think we have another issue with regard to the IRS, and that is, obviously, they are now focused on being more customer service oriented. At the same point in time, we have to be careful that the pendulum doesn't swing too far at the IRS. And we are very concerned that they still need to understand that they have to assure compliance with the Nation's laws. And there has to be an equilibrium there. There has to be an appropriate balance in doing that.

Mr. GUTKNECHT. But, again, to the question of accountability, A, were we able to recover any of that \$640 million? And if so, how much? And then, secondly, were there any repercussions to people who may have been involved in perpetrating what sounds to me like fraud?

Mr. WALKER. My understanding is no, they have not been able to recover very much. I don't know about the issue of whether or not the individuals have been prosecuted.

I will tell you this, that there are certain circumstances in which where people have participated in schemes—I gave you one example of a Medicare scheme where the beneficiary actually got a kick-back, and a decision was made for various reasons—and I don't know all the details; you may want to ask June Gibbs Brown—not to prosecute the beneficiaries.

So I think one of the things we have to ask ourselves is what kind of transparency, what kind of accountability systems are we going to have, because everybody likes accountability until they are the ones being held accountable. But sooner or later we have got to do that.

Mr. STEINHOFF. The IRS is another area that really faces major systems problems. You asked about FAA before. One of the big challenges IRS faces now is the tax systems modernization. So many times they don't have good day-to-day information with

which to manage, and they have spent large sums of money in the past on modernizations that haven't worked.

Mr. GUTKNECHT. Well, on the FAA, coming back to that for a minute—and I know my time has about expired here. It just seems to me we need to get some kind of comparison with how the private sector would do something like this.

When you think about it, essentially what the FAA does is they route and control a relatively limited number of items going from one place to the next. You compare that to what the regional telephone companies do, for example, where they are routing literally billions of pieces of information and doing it instantly. You would think for \$42 billion we could come up with a system relatively quickly that would manage the system much more efficiently than we do today. And somehow it seems to me they don't reach out, as perhaps they should, to the private sector for some expertise which is already out there.

Mr. WALKER. And it is not just the FAA. One of the things that I mentioned to you before that we are working on is we are working on identifying commercial best practices for acquisitions and for development, whether it be IT, whether it be weapons systems, or whatever else. And you are right, there is a lot to learn from the private sector, and we ought to not only encourage, in some cases we ought to require that those practices be followed, unless there is a clear and compelling reason not to, such as a credible national security threat that is a near-term threat.

Mr. GUTKNECHT. Well, Mr. Chairman, I don't want to be a fault finder, and, you know, it is easy to make headlines and demagogue some of this stuff. I do hope, though, that this will not be the last of these hearings. I hope it will be the first. I would hope that we will work with both the inspectors general as well as the General Accounting Office and try to get to the bottom of this and help some of these agencies develop systems which are more accountable. We owe it to every taxpayer. When you think about how hard some of the people that we work for work every day to pay their taxes to the Federal Government, we do have a moral obligation to make certain that they at least get their money's worth. And there will always be a certain amount of fraud and mismanagement in any entity, but it strikes me that even with the improvements that may have been made in some departments, we still have a huge problem, and we have got to stay on it all the time.

Thank you, Mr. Chairman. I yield back.

Chairman KASICH. Mr. Davis.

Mr. DAVIS. Thank you, Mr. Chairman, for holding this hearing.

I think it is important to acknowledge our role in this problem, and let me start by describing what I think is becoming an alarming trend, and that is the level of earmarking that we are directly responsible for, Mr. Chairman. This just happens to be the VA-HUD bill, and I am not going to take the time to read through this, but let me just give you one statistic that I think we all should be ashamed of. That is, in the Labor-HHS bill that passed last year, which I voted against as part of the omnibus, the level of earmarking in that bill was twice as much as the year before. The year before, the earmarking in that part of the bill was twice as much as the year before.

That is adding up to real money, and it is unraveling what fiscal discipline has gotten us to surpluses. And it is something we all bear responsibility for and we all should be alarmed about. Congress is engaging in a very disturbing trend as far as earmarking is concerned.

I want to talk briefly about Medicare and Medicaid, and also welcome our Comptroller General. It is great to have another prominent Floridian engaged in such an important responsibility.

Let me start by telling a story that I think we all should remember. There was a fellow in Miami who was in the durable medical equipment business. He was a former convicted drug smuggler. He billed the State of Florida for \$2 million in Medicaid for something that was never provided to anyone. And when they arrested him, he said the reason he was in the business was that it was more profitable and less risky than smuggling drugs.

Now, that is a true story, and it is an important lesson, because we have created a system where there are enormous temptations to people like him.

Now, the good news is that one of the lessons the State of Florida drew from that was to develop a surety bond, a criminal background check, and on-site inspections that have resulted in significant savings in the Medicaid program in the State of Florida at a relatively modest administrative cost.

A number of us supported legislation that adopted those same changes for the Medicare program, which is equally susceptible, and I am very disturbed to see in the inspector general's report today from HHS that those changes that were adopted in 1997 have still not been implemented.

I really think that is inexcusable, and I hope that we can talk further about how we can get those fully implemented, because it is a very simple example of a way to stop that from happening again in the Medicare program.

Mr. Walker, I would like you to comment, if you could, on some of the choices and tools that are available to us and where we should be focusing our attention on further attacking the problem. We have become heavily reliant on the False Claims Act. There has been legislation up here to substantially weaken that act. In reaction to that, the Attorney General has developed a memo for U.S. Attorneys which I think was a very prudent memo in terms of using this very, very powerful tool effectively.

Incidentally, Mr. Chairman, this law was passed in response to contractors' providing inappropriate materials to build cannon balls during the Civil War. So this tool has been available for a long time.

The inspector general of HHS testified last year in a Senate hearing I participated in that one of the problems particularly in the home health care area was that we were so focused on administrative costs, as we all are, that we were underfunding oversight over the home health care program.

One of the other questions that we ought to ask: Is there a way to more actively involve consumers in policing this? As the chairman alluded to, when you have got a third-party system, it is quite difficult, but we have a lot of baby boomers who are certainly capable of reading bills and understand that it is their tax dollars that

are lost when their aging relatives or themselves are being billed inappropriately. And I certainly hear from those folks.

On the criminal prosecution front, we all take great pleasure in the level of criminal prosecutions, and in my home, Tampa, we have had some of the major criminal prosecutions in this country in Medicare fraud.

But I think we have to ask ourselves the question: What has been the level of restitution in these cases? Has this been something that has been good for the taxpayer, or has it just been a way for us to feel good about putting bad guys in jail and keeping them from doing it again?

Two other points. What other lessons can we draw from the States? Mr. Walker, I happened to mention one in my home State, Florida, about the surety bonds. Perhaps the States can help us find some other ways to deal with this, particularly in the Medicaid program where they are losing their tax dollars, too.

And, finally, with the advent of electronic commerce, since so much of what we are talking about here is information management, is the technology going to help us find ways to better skin the cat here?

Mr. WALKER. Well, first, Congressman, as Willie Sutton said when he was asked why did he rob banks, he said, "Because that is where the money is." Now, if you look at what percentage of our economy is dedicated to health care, you understand why there is a lot of fraud and abuse associated with health care, because that is where a lot of the money is.

The fact of the matter is I think Congress needs to focus on a few programs or a few areas to try to be able to have impact. For example, acquisition reform. We have talked about the fact that we have fundamental acquisition reform problems, whether it be FAA as it relates to its systems, or whether it be DOD with regard to its acquisitions and other areas. That is an area.

Repayment incentives. We talked about the fact that there are a number of people that get overpaid. They are not even required by the law to send the money back. In fact, we have got a law on the books that says if there is not a prompt payment, we have got to pay interest. On the other hand, if we overpay, they don't have to pay it back. They don't have to tell us that we have overpaid, and, in fact, when they send the money back, they don't even have to pay interest or a penalty. Now, that doesn't make a whole lot of sense. There is not a level playing field there.

In addition, I think that we have to look at performance measures. Under the Government Performance and Results Act, we need to make sure that the departments and agencies are focusing on performance plans that include these high-risk areas and areas that need attention.

I think we need to increase visibility and transparency as it relates to certain costs, such as health care costs, such that people can have a better idea as to whether or not people are billing for things that weren't provided or whether they are billing for things twice.

So I think there are a number of things, but I think ultimately it is focus. There is a lot. You can't do it all at once. You need to focus on a few things. But I think that the Customs experience has

showed that if that happens—and, frankly, the Y2K experience shows that if there is a focus by the executive branch and the legislative branch on a key issue, we can get results.

Mr. DAVIS. Thank you.

Chairman KASICH. Mr. Knollenberg.

Mr. KNOLLENBERG. Mr. Chairman, if I might, I have a unanimous consent request to submit some questions, not to the current testifier, Mr. Walker, but rather to Ms. Gaffney, and I must leave the area now. So if it would be appropriate, I would like to have the courtesy of having that made available to me so we can do that. And I will make sure that they get the specific questions.

Thank you very much, Mr. Chairman. I appreciate it.

Chairman KASICH. Without objection.

[The questions of Congressman Joe Knollenberg follow:]

PREPARED QUESTIONS FROM HON. JOE KNOLLENBERG, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN

Questions for the Record for Susan M. Gaffney, Inspector General for HUD

I want to mention a few examples of waste, fraud, and abuse right in my own backyard of Detroit and get your comments on whether they are symptomatic of larger concerns within the agency.

The examples I am going to cite are from a project called “The Villages at Parkside” in Detroit, which has turned into the poster-child for mismanagement and cost overruns.

The first concern I have is about the spiraling cost of this project, which has been funded by HUD’s HOPE VI initiative. Depending upon whom you talk to, prices range from \$217,000 per unit to \$297,000 per unit. I don’t need to tell you that this is a lot of money. In fact, the renovation of a single unit cost more than many of the homes in my district! But no one is sure because the books are in such poor shape.

Federal auditors have said that the cost of these homes should be no more than \$150,000 apiece. Such costs may be unprecedented for the HOPE VI program and, frankly, it is outrageous that the price tag may be double due to the mismanagement by the Detroit Housing Commission (DHC).

Further compounding this is the fact that many of the contractors who have worked on the Villages at Parkside still have not been paid for their services. I’m aware of a contractor who is now having serious problems meeting their payroll because the Detroit Housing Commission has misspent the funds and can’t pay them. This contractor is not alone—there are other contractors who are having payment problems with this agency. This concerns me a great deal.

I’m also very concerned about the DHC’s handling of the bid process for the Villages at Parkside. I’m aware of a contractor who was told by the agency that they could submit their bid proposal an hour late after taking a wrong turn in driving it to the headquarters. The contractor subsequently had their bid returned—unopened—and rejected because it was submitted after the deadline. Aside from the fact that this company’s proposal turned out to be 10 percent less than the successful bids, I think this raises serious concerns about the agency’s procurement process. Accepting a bid proposal is the most basic of tasks and the Detroit Housing Commission can’t even get it right.

The entire process for the Villages at Parkside has been a debacle. From soliciting bids to paying contractors to cost overruns, this project has been a complete disaster for the taxpayers from the beginning.

I’m not the only one concerned about the mismanagement for the Villages at Parkside, the Detroit Housing Commission, and HUD’s oversight of the local agency. The Detroit Free Press has published a series of articles exposing this debacle, rampant mismanagement from the locals, and the relaxed oversight from HUD.

In fact, the latest installment was published on February 16, 2000, under the title, “Housing Rehab Plans Crumbling” (page B1). It details how the Villages at Parkside are \$7.5 million over budget and the situation has been so badly mismanaged that the project must be significantly scaled back.

I know the examples I just outlined are specific to Michigan and that you may not be familiar with the particulars of these situations, but I suspect they are symptomatic of larger problems.

Question 1: Do you have any reaction or comment to the examples I have just raised?

Question 2: Does HUD have an oversight mechanism in place by which it can remedy these situations? If so, what are they?

Question 3: Are these examples symptomatic of larger problems for public housing? If so, please elaborate.

Question 4: In your opinion, will HUD's "Management 20/20" reform plan alleviate or remedy such problems?

Question 5: In your opinion, will any program HUD administers alleviate or remedy such problems?

Question 6: What can Congress do to ensure that such egregious examples do not occur again?

Chairman KASICH. Mr. Sununu.

Mr. SUNUNU. Thank you, Mr. Chairman.

Thank you for being here, Mr. Walker. I want to focus on the Department of Housing and talk about a number of the problems that have been identified, perhaps some of the progress that has been made in the particular areas of high risk, and talk about what you may see as opportunities for making more progress.

Let me begin by talking about a point you made with regard to the 2020 program. One of the opportunities that they identified for improving their performance was to reduce the total number of programs. And although I sit on the VA-HUD Subcommittee, I must admit I don't know exactly how many programs they administer currently. If you could perhaps enlighten us somewhat, what is the approximate number of programs being managed within housing? Have they achieved their goal of reducing the number of programs? And, finally, are there any opportunities that you see that are very straightforward where programs could be consolidated with little or essentially no impact to the customer?

Mr. WALKER. An introductory comment, and then I will ask Keith Fultz to address some more details.

HUD has their 2020 plan, which is a framework that, if properly implemented, will achieve positive results. And that in and of itself is good, but we have got a ways to go before we are going to get those results.

One of the things they need to do is they need to focus more. They have too many things going on, and they need to make sure that they have the right people with the right skills in those areas.

Mr. SUNUNU. If I may interrupt, I want to talk more about that—the personnel issue and focus within specific programs are in some ways a separate question. If you could at least begin by addressing the question of absolute number of programs and, by definition, what impact this has on administrative costs.

Mr. FULTZ. Right. The number of programs they operate are in the high 200s, and they have been going through a process of reducing and consolidating, so it would be difficult to give a precise number at this time. But the number clearly is into the high—

Mr. SUNUNU. Has there been a reduction over the past 2 to 3 years?

Mr. FULTZ. Yes, there has been. They have consolidated activities, placed responsibility and accountability, which they did not have, as the Comptroller General has mentioned before, which is extremely important. When we first started to look seriously at the management of HUD, which goes back into the early 1980s and maybe even beyond, we found that staff had no accountability or

clear lines of responsibility. Managers did not know what they were basically expected to do.

Mr. SUNUNU. In which areas of their current operations do you see the greatest additional opportunity for consolidation?

Mr. FULTZ. Well, when we first identified HUD as a high-risk agency with the programs they were responsible for, they had basically 81 field offices that were directly responsible for managing all the various aspects of HUD. What they have done, in accordance with their 2020 plan, is to take those offices and functions and consolidate and centralize by functional areas, like financial management, physical inspection of the properties, accountability, into key central offices that have responsibility for overseeing all of the HUD programs, including Section 8. The entire operation of HUD is going through a very tremendous change in centralizing and consolidating.

Mr. WALKER. But what else should they do?

Mr. FULTZ. What else should they do? They need to do a better job of inspecting their properties. They need to do a better job—

Mr. SUNUNU. I am sorry to interrupt. What areas, what opportunities are there for further program consolidation? I mean, 250 programs, that is still stunning. Whether it has been reduced from 280 to 250 or from 400 to 250, I think most Members of Congress, let alone most Americans, would be surprised to hear that the number is so high. There has to be opportunity—

Mr. FULTZ. There are opportunities, and we, in fact, are looking at that right now, and that is one of the issues that we will be addressing and will be part of our decision as to whether or not the programs at HUD remain on the high-risk list. I could provide some detailed information.

Mr. SUNUNU. If you could provide the committee with a summary of the various programs broken down by HUD function, I think that would give us a much clearer picture of where the opportunities for performance improvement might lie.

Mr. FULTZ. We will do that.

Mr. SUNUNU. If we could continue, talking a little bit more about performance, and this sounds like an area where there has been an attempt to improve, but it has been somewhat ineffectual. It is my understanding that as part of the 2020 they have tried to implement a new procurement model. But it really only ended up reviewing one procurement action out of 150 or so that were taken in 1999.

Why have they been so ineffective in reviewing procurement? And I assume that those reviews are intended to avoid the kinds of problems we heard about in DOD. Could you talk a little bit about the procurement board and what needs to be done?

Mr. FULTZ. It goes back to the issue of financial systems, management systems, which were not fully integrated, and they are addressing that in their procurement activity, and once again, that is an area where they are working on it, and I think the jury is still out as to how successful that will be.

Mr. SUNUNU. Have they set a goal for doing a little bit better than 1 out of 150?

Mr. FULTZ. They have improved their goal, yes, and they are making performance measures—

Mr. SUNUNU. What is the goal? Do you know what the goal is?

Mr. FULTZ. I frankly don't know what that goal is today, but, again, as a result of the Performance and Review Act, where agencies are required to place performance measures, is an area that is helping HUD as well as other agencies in making better and informed decisions. This will also provide the Congress with the oversight data that you need to make judgments about how well they are doing.

Mr. SUNUNU. I want to talk about personnel focus. Mr. Walker began speaking about it briefly, and, unfortunately, it is another area where performance has been, I think—has represented a very ineffectual use of taxpayer dollars.

The community builder program. First, I think it was your audit or set of interviews that showed that two-thirds of those in the community builder program spend more than half their time doing PR work, which is an enormous problem in and of itself because clearly that means people are spending time on a program or work that isn't part of the agency's core mission.

Second, this committee, in working with people from HUD, has come to realize that most of the community builders don't have any experience in the areas where they are supposed to be working in the first place, that they don't have the background in housing, and as a result even if they were working on housing programs, really haven't served the taxpayers well.

Could you comment about those statistics, the interviews that you did, and the weaknesses in this program?

Mr. WALKER. Let me comment first, and then I will turn it to Keith.

Clearly, we have said that community builders were focused on the type of activities you were talking about, Mr. Sununu, and clearly one of the things that HUD needs to do, it needs to focus more resources on oversight. Community builders may or may not be a good idea, but the bottom line is you have got a finite amount of resources, and their basic need is to have people focused on oversight.

Keith.

Mr. FULTZ. That is correct, and the figures and statistics that you stated are correct. And that was one of the major issues that we addressed in our reports on HUD, the organizational structure as well as their staff mix and the training and development that they were providing their staff. They just weren't operating and weren't training their staff the way they needed to be doing.

Mr. WALKER. And the kind of people that you need to do oversight are fundamentally different than the type of people you need to do community outreach. And that is part of the skills, having the right kind of people focused on the right thing with the right skills.

Mr. SUNUNU. My last question is about the FHA property inventory, and I have heard some officials from HUD suggest they are making quick progress here. But I see some alarming statistics: an increase in the absolute inventory from 24,000 or 25,000 properties, to over 42,000, an increase in the number of defaults, and an increase in the average loss on these properties.

It appears to me that performance is deteriorating, that the taxpayers are being put on a hook whose size is ever increasing on a

daily basis. Could you talk about that deteriorating performance? And maybe point to which of these statistics we should look at most closely in gauging any improvement in the future as well.

Mr. FULTZ. Yes, I will. You are correct. The number in the inventory is increasing—in fact, it is approaching in the 40,000 number now, and that is up from the 24 figures that you provided. The average cost to the Federal Government once these properties are foreclosed, is about \$30,000 per property. So the inventory approximately at this time of which the Government is susceptible to losing is two—I believe it is \$2.2 billion, and that program is under revision by HUD. They have hired contractors to manage those. There have, in fact, been problems with some of those contractors.

Mr. SUNUNU. This is the contractor that went bankrupt, had half of the market—

Mr. FULTZ. This is the—

Mr. WALKER. Forty percent.

Mr. FULTZ. Forty percent of the inventory which they were handling, and they were doing a very poor job of managing and marketing those properties, which would, in effect, result in your suggestion that the Government could lose more money, because if the properties aren't maintained, if they are not secured, then they don't sell. And that is what we are facing.

That would be an area that I would be paying attention to, and we are, in fact, reviewing that program as we speak.

Chairman KASICH. Mr. Holt is recognized.

Mr. SUNUNU. Thank you, Mr. Chairman.

Mr. HOLT. Thank you, Mr. Chairman, and thank you, Mr. Walker, for good testimony.

I would also like to thank the chairman for stating that the goal of today's hearing is not to paint the agencies as the enemy. I think it is important that we all understand that if the Government is the enemy, then we, the people, are painting ourselves as the enemy. And that is not the case.

There is, I think, a lot of responsibility, as Mr. Davis pointed out, that rests right here in the Capitol as well, not just to limit earmarking but in the way that we put together our budget each year, too. I know Mr. Jack Lew has said that it will take years for OMB to untangle all the budget gimmicks that have been applied to appropriations for the various agencies, and so I think there is a lot we have to do there.

Also, you have spoken, Mr. Walker, about the number of occasions where repeated flood victims are bailed out. And you refer in your testimony also to the mining law of 1872 that requires miners to pay no royalties to the Government for hard rock minerals extracted.

And one somewhat smaller but, I think, symptomatic case that is not minor, has come to my attention through a study that I asked the Government Committee to undertake. In Medicare we are spending a great deal of money, I would say wasting a great deal of money, because Medicare will reimburse injectible versions of some medicines and not the tablet form.

Take the case of hemodialysis patients. Hemodialysis patients must take calcium supplements. Medicare will not pay for the tablet form, but they will pay for the much more expensive injectable

form, and as a result the Government is spending \$103 million a year, it appears unnecessary, and the patients themselves are spending \$30 million a year in copayments. So there are some things that Congress does that force the agencies to do what you are talking about today.

To return to some questions that were raised earlier, there was some discussion about the earned income tax credit payments. It is my understanding that Treasury says that all tax credits, including EITC, account for only about 6 percent of total tax avoidance. If the IRS were to hire more auditors, would it be a good idea to devote those auditors to EITC and other tax credits, or perhaps to corporate noncompliance or other high-income noncompliance?

Mr. WALKER. Let me mention first that I don't know when that estimate was done, but I can tell you that one of the concerns that we have is that the IRS is not focusing enough on tax avoidance and tax compliance in the last couple of years. But with regard to your specific question, Jeff.

Mr. STEINHOFF. With respect to the earned income tax credit cases, it gets back somewhat to a human capital issue if you are speaking about shifting resources. Those people basically have the skills to handle that type of case and could not probably take on a more complex corporate case, which is much, much different.

Mr. HOLT. OK. Changing to a different subject, in the Department of Education, there were some years back lots of charges about the inefficiencies or downright fraud in the student loan program. What can you say about default rates today and about the performance of the Department of Education in tightening controls there?

Mr. WALKER. Well, default rates have gotten better. Vic.

Mr. REZENDES. Yes. The current default rate now is a little over 8 percent. In the early 1990s, it was about 20 percent. And Education has also been aggressive in recovering previous default monies. I think just a couple years ago it was like \$2 billion in cost recoveries.

Mr. HOLT. And general comments about the efforts to tighten up?

Mr. REZENDES. Yes. They are instituting processes and checks in place. I think the big one is still the match with the IRS, and that is still to be determined. We talked about that earlier. And the difficulty there is IRS is looking for legislative relief from the Congress to help out there.

Mr. WALKER. It is an IRS problem.

Mr. HOLT. Well, thank you. I see my time has expired. I will just make the comment, by the way, that I have introduced a legislative remedy for this Medicare kidney dialysis problem that I referred to earlier.

Mr. Chairman, thank you.

Chairman KASICH. Thank you, Mr. Holt.

Mr. Thornberry.

Mr. THORNBERRY. Thank you, Mr. Chairman.

Mr. Walker, I particularly appreciate your emphasis on trying to root out the systemic problems because there is no way that we can legislate away mistakes or criminal behavior. But in some ways, the most distressing idea to me is that the Government moves

sleepily along its path, nobody really in control, wasting and abusing money left and right.

I want to try to understand, getting back to this one example that you brought up on the trailers. As I understood your testimony, the Army decides it needs a trailer, and somebody comes up with the specifications for how big, how wide, how deep, what kind of axle it has got to have, and then it went out and bought some of these without testing to see whether that would meet their needs. Is that essentially what happened?

Mr. WALKER. Right. It was a failure in testing. They did not do adequate testing before it went into production.

Mr. THORNBERRY. They did some testing, but they didn't do adequate testing.

Mr. WALKER. Right, they didn't do enough before they committed to production.

Mr. THORNBERRY. Was there some sort of a time pressure to get these in the field right away because we were not going to be able to transport battle equipment unless we had them out there?

Mr. HINTON. No, sir. There was no pressure, no time lines. What was at work here, sir, was you had a set amount of money that you had in procurement dollars that needed to get obligated on contract, and that kind of goes to the heart of the systemic issue here. It is the competition of funds within the Department.

Mr. THORNBERRY. So this is a "spend it or lose it" sort of situation that we have heard about in the Federal Government for years.

Mr. HINTON. Correct.

Mr. THORNBERRY. And that is why things like this occur. It is not really a testing issue as much as it is—

Mr. WALKER. Well, but they are related. They are related. Because the concern is if you don't spend it, you are going to lose it, and, therefore, you do shortcuts such that you can then obligate the money.

Mr. THORNBERRY. To get the money out the door.

Mr. WALKER. Correct. Obligated.

Mr. THORNBERRY. When you look at your commercial practices, will you have suggestions for us on how we can move the incentive the other way to spend the money smartly not just to get it out the door?

Mr. WALKER. We will have a number of commercial best practices that will be in our report which we think will provide a good foundation and some recommendations as to what the Congress should consider and, frankly, the executive branch should consider.

Mr. THORNBERRY. And dealing in part with this problem?

Mr. HINTON. Yes, sir. And it goes all the way across the entire process, and we have broken the process down, like quality assurance, testing and evaluation, requirements determination, when do you insert technology as opposed to rushing into production. And we have gone out and done best practices work and are working with DOD to build that into some of their acquisition guidance.

Mr. THORNBERRY. Do you happen to know whether there was a commercial trailer available which could have met this need?

Mr. HINTON. There was not at the time a commercial trailer. There was one that had been previously designed for another mili-

tary need and the Army attempted to adapt it to their current need.

Mr. THORNBERRY. OK. I don't know if this is possible in your best commercial practices work or not, but about as distressing to me as the cost on some of these things is the time it takes to get equipment deployed to the people who really need it, particularly as rapidly as technology changes, not with trailers but with nearly everything else we have got with computer chips and stuff. And I hope that these better practices can also shorten the time that it takes to—

Mr. HINTON. Yes, sir. That is one objective, and that is what our research has shown, that if you change some of your business practices, you can move things along much quicker, less cost, and actually put yourself in the position to make sure that what you are buying gets the job done.

Mr. WALKER. Yes, improved quality and performance.

Mr. HINTON. Absolutely.

Mr. THORNBERRY. This is a basic question I guess I don't understand, and it is not just Department of Defense. How can there be, as I think your report said, something like \$24 billion in unreconciled transactions? How can we send that much money out the door and basically not know where it went? There has got to be a purchase order, a contract associated with it, or something. And I see with defense that a fair amount of money goes without a valid contract attached to it, and all of these—how can that happen? It is kind of like the chairman's "How can this be?" question.

Mr. WALKER. Well, the problem is not necessarily where it went, but who it gets charged to, and having the appropriate documentation to support the expenditure in order to be able to make that allocation. Jeff.

Mr. STEINHOFF. DOD has a very complex accounting operation. The Comptroller General mentioned before the lack of integrated systems, the complexity of it. And what happens is a payment is made. It then has to be matched up against an obligation. It is not done automatically through a system, and you have very complex accounting codes where you might have 100 or 120 digits related to an item to account for it.

So, it gets into the wrong queue at some point in time and it must be reconciled.

Mr. THORNBERRY. And you can't go back and figure out what went wrong.

Mr. STEINHOFF. It is very hard to do it.

Mr. THORNBERRY. I see.

Mr. STEINHOFF. And your focus is on paying the next amount and the next amount because you want to make your vendors whole.

Mr. WALKER. And on the Prompt Payment Act there are actually penalties if we don't pay on time.

Mr. THORNBERRY. Well, is this one of those areas where we need to make an investment to get them a new computer system or a new software or something to be able to talk with one another and not have 100 digits to sort through, to code a payment?

Mr. WALKER. We need to have the design specs down before we give money. I think one of the problems is that in some cases there

may need to be targeted investments, so, this may well be one. But we need to make sure that they got the right kind of plan in place so that they are going to prudently spend those dollars before you just give the dollars.

Mr. STEINHOFF. They have to really basically reengineer a lot of their business processes, which they are now trying to do in earnest. Maybe they can use electronic commerce, a swipe card for instance to make payment, whereby you would pay for an item and then it would automatically go to the accounting records. You have to have an integration of the program and accounting systems.

Technology would be a facilitator but that must be planned out very well before you go ahead with it.

Mr. WALKER. And you don't want to automate DoD's current processes.

Mr. THORNBERRY. Right.

Mr. WALKER. You need to reengineer the processes, streamline the processes before you try to automate or else you got two nightmares.

Mr. THORNBERRY. Let me ask you about one other area. I see some references to a growing concern about fraud and DoD health care. That is an area that a lot of folks in Congress have spent a lot of time and concern about that it is not enough to meet the needs or meet the promises that we have made in the past, and the idea that there is deliberate fraud or waste is very distressing.

Can you tell me what the size of the problem is and what the nature of that problem is?

Mr. WALKER. I don't know that I have an estimate. I will ask Vic. I will tell you it is not just a matter of efficiency, it is also a matter of who is getting the health care. And in some cases, the health care is being provided to portions of beneficiaries that it wasn't intended to be being provided to because we have got excess capacity in the VA system that people are trying to use up this capacity and justify what they have.

I mean, for example, we have got infrastructure in VA that is multiple times what they really need. We have got a lot of duplication between different types of health care providers in Government.

Mr. REZENDES. He is exactly right. Both in the DoD and in the VA system there is excess capacity. Especially looking at how the demographics of the military population has changed, including those on active duty. Most of the people we are providing medical coverage to are retirees, not active duty people.

There are a number of efforts underway to get them into more managed care, TRICARE and various other kinds of things. And when you get into managed care you run into the same kinds of fraud problems as you would in any kind of medical system.

Mr. THORNBERRY. So, is it worse than managed care in the civilian sector? Is it about the same? Or do you—

Mr. REZENDES. I couldn't even guess.

Mr. THORNBERRY. OK. Thank you.

Chairman KASICH. Let me just say to the gentleman from Texas, who I know has become increasingly frustrated with what he has observed over in his other committee, that I think this committee is going to proceed probably by breaking up into task forces.

And what we will attempt to do is to have members on both sides in a task force so that we can narrow down these issues to find out which of these things are legitimate, which of these things are hype. There is no question you are going to be on the defense task force. If I had my way you would be chairman of it, we will see.

But we hope to break this down so that we can carefully scrutinize all of these areas and spend this year just staying on top of things. It is a good role for the Budget Committee now that we have balanced this budget and can be a center point of these things.

I think next is Mr. Price, the gentleman from North Carolina.

Mr. PRICE. Thank you, Mr. Chairman.

Mr. Walker, welcome. I want to commend you on your testimony and on all the good work that lies behind it. I am particularly glad to see you focusing on the issue of Medicare fraud. As you know, that is of particular interest to the committee and the Congress. And I think it is entirely appropriate that you focus on the outrageous and often criminal behavior that has defrauded beneficiaries of that program and the American taxpayer.

We are struggling to fund Medicare. We are struggling to extend Medicare's solvency. We are struggling to cover the legitimate costs. And we need to struggle to expand Medicare and improve Medicare and particularly to include prescription drug coverage.

So, it is just deeply frustrating to find that funds have been siphoned off through fraud. That is a profound disservice to those who depend on that program and to the taxpaying public and also to the providers. Because of the need to root out fraud providers often have to be hassled to do more paperwork, to provide more evidence,-- legitimate providers. And, of course, that is another price we pay for the few who abuse this program.

So, I appreciate your focus on that and I take some encouragement at the progress we have made. Although I want to turn to another department in my limited question time here, I do want to make note of that 45 percent reduction in the Medicare payment error rate. I want to ask you for the record, if you will, to provide an answer, that is assuming some other member doesn't raise the question. If you could, let us know to what you attribute the dramatic reduction in the Medicare payment error rate and also perhaps back up a bit and give us an assessment of the claims processing controls; how they work, which ones do work, which kinds of controls work in detecting fraud and abuse, which controls are inadequate or are not worth the effort that we put into them. Help us, if you will, with a report on the techniques you are using there, the tactics you are using and how, and what next steps you envision?

Let me turn to the Housing and Urban Development Department for an oral response here, if I might, because here, too, we have programs that our constituents depend on. I would ask you especially about the Section 8 program. In my district many, many people -- low-income people, disabled people -- depend on that program. There are never enough Section 8 slots and that is partly a matter of not having the certificates and partly a matter of not having the participating properties. But we need to, of course,

make certain that that program is benefitting the maximum number of people in need.

And, so, we want to make sure those dollars are being properly spent and properly directed. And as you know, there were some negative findings back in a GAO report in fiscal year 1998 about excess housing subsidy payments -- something like \$857 million, I think you found, out of an \$18 billion total, this, of course, is way too high.

I do understand though that HUD has moved to try to rectify some of these problems and I would like to have your assessment of the adequacy of those mechanisms and any progress or lack of progress that you would want to comment on that we have made so far.

In particular, we have the sample-based audits. They have proceeded from or moved beyond the paper-only, sample-based audits using dated Social Security information to a fully automated data management system. There is this new real estate assessment center which is matching up the Social Security and the IRS data to determine tenant eligibility and underreporting. And we have the tenant income verification system within the REAC which is aimed at stopping fraud.

What kind of assessment would you give of the Department's response to these earlier findings, particularly in this area of Section 8 and tenant fraud?

Mr. WALKER. A couple of things. First, that work on Section 8 actually was a combined effort, I believe, of GAO and the Inspector General. Secondly, we currently have a review under way of a number of different, of our outstanding recommendations, with HUD and the status of where they stand that cause them to be on high-risk.

For example, I have a draft letter that I probably plan to send to Secretary Cuomo within the next few days that is based on a meeting that I had with him within the last month that summarizes all outstanding recommendations that GAO has with HUD in order for them to make sure that they are focusing their efforts.

And I would ask for Keith Fultz to comment on the Section 8 status.

Mr. FULTZ. I would say that they have made substantial progress. The area that I would be concerned about is the internal controls and making sure that there are mechanisms for reporting the income in this particular program. As you know, it is 30 percent of the income and that is where the subsidy kicks in. And I believe HUD and the Inspector General have done some work in this area, has identified the internal controls and how that reporting mechanism is working in the systems that you described. It is still, in my opinion, in the early stages of implementation and the results are yet to come.

Mr. PRICE. I appreciate that answer, and realize it is too early to ask for a kind of comprehensive assessment of this. But do the mechanisms seem to be well-designed to achieve the desired result?

Mr. FULTZ. From what we have looked at, yes, they are.

Mr. PRICE. Now, I think it is interesting that the HUD IG's report that we are going to be hearing later today—and I regret, too, Mr. Chairman, that I will not be around this afternoon— although

it is quite lengthy and relentlessly critical, really gives no very detailed account of this effort at correcting these problems within the agency.

And since I won't be here this afternoon, I want to make one comment about this. This IG's report is pretty negative, and doesn't seem to give much attention to the more constructive efforts that are underway and there is one phrase that jumps out at me here. The IG at one point sarcastically refers to the Secretary as "Mr. Clean". Now, Mr. Walker, does that strike you as good professional practice? Would you do that sort of thing in a report on an agency?

Mr. WALKER. Well, I really wouldn't want to engage in a peer review of a fellow accountability professional. I will say this, we at GAO have certain core values: Accountability, which is what we do; integrity, which is how we do it; and reliability is how we want to be received. With regard to integrity, we want to be professional, objective, fact-based, nonpartisan, nonideological, fair and balanced. That means that we understand we work for the Congress, we are a watchdog, we want to find out where the problems are. And, on the other hand, if progress is being made we want to acknowledge it and we think that is important. Because the ultimate objective is to get a positive result. And the ultimate objective is to solve the problem for the benefit of the taxpayers and frankly to try to help improve the public's confidence in and respect for their Government. You would have to ask the Inspector General.

Mr. PRICE. Is she in the room, Mr. Chairman? I don't want to make an unfair comment. If she would like to explain why she refers to the Secretary as "Mr. Clean" I would be happy to hear the answer.

Chairman KASICH. Does the gentlelady want to take the microphone? This is highly unusual. But go ahead, if you want to respond, use that microphone, Ma'am.

Ms. GAFFNEY. I did not intend to refer to the Secretary as "Mr. Clean". You know the "Mr. Clean" that used to appear on household detergent cleaners from Proctor and Gamble? It was my understanding that that person, "Mr. Clean", showed up at the celebration. I had no intention of referring to the Secretary.

Mr. Price, on the question of the matching, it has been about 9 years that we have been reporting this income verification problem. This year, for the first time, we truly see progress being made. That is in my statement.

Mr. PRICE. Where, in that statement, does that occur?

Chairman KASICH. I think the gentlelady is not under oath here.

Mr. PRICE. For the record, if you could reference that?

Chairman KASICH. She is going to be here to testify but you are going to have to go, so, we will make sure that if you have your staff here and listen to what the gentlelady has to say.

But I remember "Mr. Clean". I think he came on in commercials in between the "Petty Coat Junction." [Laughter.]

OK. The gentleman from California is recognized.

Mr. MILLER. Thank you, Mr. Chairman.

I have some questions for HUD. And we have had a lot of words used today: inefficiencies, fraud, mistakes, criminal behavior, Government is not the enemy, we should not attack Government because we are the Government.

I want to preface my questions with a story. We have heard a lot of stories. It was about two fellows that were general contractors. One was probably 21, 22, the other was probably 40, 41. Back in 1970 and 1971, they were put on the approved contractor's list for HUD where they could bid HUD programs in the L.A. area. And they were bidding work in East L.A. and as they started bidding work every time a bid would come up they tended to be the low bidder. And they started to get a large quantity of low-bid approvals from HUD and they were put on the list accordingly. And they started to do the work and they were doing good work and kept bidding RFPs, and there was quite a few other contractors involved in that area. And they were taking a lot of the work because they were bidding at a better price than their competitors were.

I probably could say that this story would be called a bureaucrat's worst nightmare come true and I think you will find out why. All of a sudden one day the local director for HUD called the partner in, who was in his early 40s, and told him—and you understand how HUD work was broken down at that time, you had to list the costs of each associated task, list your overhead, and you had to list your profits separately. And your profits generally were about 30 percent of the HUD bid at that point.

The director told the one partner that if they wanted to bid any more HUD work he would have to give the director a third of the profits in cash prior to the contract being let. Well, the older partner came back to the younger partner who was in his early 20s and the younger fellow was the one doing all the bidding and actually running the work in the field. And the younger fellow, I guess he was naive, told the older fellow that the director couldn't do that, that they were on the approved bid list and they couldn't stop them from bidding on Government work, which was, in essence, probably true.

The problem was from that day forward this same company would bid RFPs for HUD, they would be low bidder but HUD always found a mistake with the RFP. And it had to be restructured and when the RFP was restructured this company was off bidding another RFP and this RFP was out to bid to some other contractors.

Well, that young contractor is a member of Congress sitting before you today. So, you have to understand I look at HUD from a different perspective. The only thing that could make this nightmare worse is if I was Secretary of HUD. It would probably be a little worse.

I have some questions. And I hope I have a little time to do this. My concern with HUD is the money they are losing by keeping large inventories of foreclosed FHA homes. Let me give you a list of a few statistics and I think they are important. And let me know if these numbers reflect a strong agency performing well in a good economy.

Federal Housing Administration, FHA Mortgage Insurance paid out 77,000 claims worth \$6 billion in 1998. That cost is passed on to consumers through higher premiums. In 1977, single family homes stayed in the Federal inventory for an average of 5.4 months, in 1998, the average time in inventory was 6.6 months, and last I checked it was still increasing.

In 1996, HUD had 25,000 single family properties in inventory. In 1998, the inventory increased to 40,000 and as of June 30, 1999, HUD had 50,000 properties in inventory. And that inventory of 50,000 homes was in a market where every other sector's inventory was almost zero.

I mean realtors were having a problem listing homes because there were none available. The HUD single family inventory was valued at \$1.9 billion in 1996, and it increased to a value of \$3.3 billion in 1998. And 15 percent of HUD's properties are held in inventory for more than 12 months. This is compared to the industry average of 2 or 3 percent, where they have an inventory of more than 12 months.

In 1996, average loss per property on HUD was \$28,000. In 1998, the average loss had increased to \$31,700, a 12 percent increase; and as of June 30, 1999, the average loss number was \$32,470. You can multiply 50,000 properties in inventory by the average loss of \$32,470 and that is \$1.6 billion.

This is not just a theoretical problem for my district and many districts throughout the country. One city I represent has over 200 properties that are boarded up that are considered HUD inventory. Local officials are frustrated with excessive amounts of boarded up properties and again my question was, do these numbers reflect a strong agency performing well in a good economy?

Mr. WALKER. Not in conjunction with that program. I mean the fact of the matter is that we have done work in this area, the Inspector General, who will be here later to testify, has done some more recent work. In order for the inventories to increase in this type of economy, obviously that tells you something about the condition of the properties, which comes back to one of the issues that we talked about earlier, and that is the need for more oversight, not just to focus on cost, but to focus on other factors that cause this inventory to rise.

And I don't know if Keith would have another comment.

Mr. FULTZ. I think the Comptroller General is right. And to the best of my knowledge the figures that you have described are accurate. And HUD has a program which they are trying to improve these issues and that is the market and management contractor's program where they have hired contractors to manage these properties. Frankly, the results of some of those contracts have not been successful.

In fact, one, as we have mentioned earlier, held about 40 percent of their inventory and because of mismanagement and financial difficulties declared bankruptcy. And those projects or those homes are now back into the inventory. Many of those homes are getting older, are deteriorating, and that is why we have recommended the need to monitor and to inspect. And the issues that you have talked about are absolutely correct.

Mr. MILLER. How would you rate HUD's system of monitoring grantees? Apparently some in HUD just continually monitor the grantees that happen to be near their offices.

Mr. WALKER. In this particular program D plus, C minus. But you might want to ask the Inspector General.

Mr. MILLER. Is that the lenient curve, too, probably right?

Mr. WALKER. You mean we are on a curved system?

Mr. MILLER. There is a curve there to give that.

Mr. WALKER. Everything is relevant.

Mr. MILLER. Another problem I have—

Chairman KASICH. Mr. Miller, we are going to have to move on. The only reason is that we have got the IGs, who are going to be here, and we have the HUD IG and we need to try to get to them before we get too late. But I don't want to discourage you.

Mr. MILLER. Thank you, Mr. Chairman.

Chairman KASICH. OK.

The gentlelady from Michigan.

Ms. RIVERS. Thank you, Mr. Chairman.

Thank you, Mr. Walker, I am very pleased to hear your report today. I am pleased to hear the thoroughness with which you have done your investigation; not as pleased to hear some of the information that you are sharing with us.

I want to ask a series of questions that really goes in a little different direction because one of the things we have been discussing as a Budget Committee and that we are going to discuss in the future is whether or not the elimination of fraud, waste and abuse can be a legitimate factor in our budget deliberations this year. In other words, whether or not the existence of fraud, waste and abuse represents a justification for lowering our discretionary spending caps.

And the thing that I am particularly interested in is whether or not we can quantify the problems that you have out there? And I ask that because I listened to you talk about problems that could be categorized as internal oversight procedural problems which may or may not create a loss. They are a problem and they need to be rectified so that you can keep track of what is going on but there may or may not be money associated with that.

You talked about problems like the trailer where there were some very bad decisions made. And some of that money could have been saved but ultimately we would have had to have made an expenditure no matter what. So, you can't simply look at the cost of this and say all of that money could be captured or be recovered.

And then you talked about other kinds of problems that could be addressed through changes in personnel, through mechanical changes, computer systems, whatever, which seemed to suggest that we would have to spend some money in the short-run to gain some money in the long-run.

So, given these different kinds of factors that exist, how reliable can you be at attempting to quantify how much of this money is recoverable as part of a budgetary process?

Mr. WALKER. I don't think that you can generalize. The fact is there are a number of different buckets here. There is fraud, waste, abuse, mismanagement, inefficiency. However, some of these represent items that will take a considerable amount of time in order to be able to resolve. It will take a partnership approach on behalf of the Legislative and Executive Branch to be able to address. In some instances, but by no means all, they might require target investments, but I do think there is a lot that can be done, quite frankly, without those targeted investments by dealing with some of these systemic issues.

But dealing with some of these systemic issues, in many cases, is going to take time.

Ms. RIVERS. Well, then how—and I hate to put you on the spot to speculate on our efficiency here, though everybody else does—how effective do you think we could be as a body trying, in the space of a 6-month budget process, to come up with a reliable number that we can plug into the budget and say, yes, we feel comfortable that this much money will be recovered in the next budget year?

Mr. WALKER. It would be extremely difficult. I mean the fact is you might be able to come up with a number and we might be able to help you come up with a number as to what the potential savings opportunities are but then you are also talking about within a horizon. If you are talking about a 1-year horizon, that would be extremely difficult.

Ms. RIVERS. OK. The other question I have is really a strategic one which is the sort of idea that by lowering overall spending we will have some sort of impact on specific problems. And the analog I would point to is Medicare where we made some changes in overall spending in an effort to get to the fraud, waste and abuse in home health care and we ended up taking a big bite out of programs where there was not fraud, waste and abuse because it was the blunt instrument of an overall cut.

What do you think the efficacy of simply making cuts in overall budgets would have on dealing with specific problems? I mean would we necessarily produce the results we want through that kind of a strategy?

Mr. WALKER. The inefficiencies and the potential for fraud, waste, abuse and mismanagement vary across Government. And even this last time, where there was an across-the-board cut, there was discretion given as to where those cuts should be taken. I think it is important to be able to target whatever cuts to the areas where you think there is the most opportunity because the efficiency varies. Fraud, waste, abuse, mismanagement varies. And those decisions should vary.

Ms. RIVERS. So, you are suggesting that if we really want to have an impact on this problem we identify specific problems and target budgetary cuts to those areas as opposed to generalized cuts within agencies?

Mr. WALKER. Ultimately you need to be able to target. How you achieve that, there are several ways to do it, but ultimately you need to achieve some targeting.

Ms. RIVERS. OK. The last question that I have, I listened with a certain bemusement to the discussion about the waste in the Department of Defense, because I can recall just not very long ago when we were finishing up last year's budget we were having a very lively discussion right here at this table about who was willing to spend more on defense. And we were busily adding dollars in after the budget process had finished.

I have been here for 6 years. Each and every year Congress has exceeded its beginning number on defense and added in weapons system and dollars at the very end of the process. Do you think that that behavior on the part of Congress has helped or hurt the

kinds of things you were discussing today relative to the Department of Defense?

Mr. WALKER. I think it has hurt. I think the fact is that there has been too much focus on the top line, there has been too much focus on symbolism, and we have not done enough work, meaning the Executive Branch, as well as some cases, the Legislative Branch, to focus on what type of return are we getting on those investments? And where are there opportunities to spend the money more wisely to be able to meet legitimate needs.

Ms. RIVERS. Great. Thank you.

Thank you, Mr. Chairman.

Chairman KASICH. Let me ask the members, if you have a compelling question we will let you ask it. I just wonder if it would be possible to move to the IGs?

Mr. BENTSEN. Mr. Chairman, I would have been here earlier but I had the Chairman of the Federal Reserve testifying before the Banking Committee and I gave him preference.

Chairman KASICH. How did he do?

Mr. BENTSEN. He did OK. Less forthcoming than this panel.

Chairman KASICH. I was just trying to get to the IGs but if you have some questions, go ahead, you are recognized.

Mr. BENTSEN. That would be great, Mr. Chairman, and I think they are on the clock so I think they are getting covered.

First of all, I want to commend you for having these hearings and the only thing I would add to it, Mr. Chairman, is in addition to having GAO and the IGs up here, I think you ought to haul the managers of the Departments up here and put them on the hot seat. A number of us, came from the private sector. I wasn't a lawyer or anything like that. But if a department head had these kind of problems they would be hauled before the board or the chairperson of the company and told to explain their overruns. So, I would encourage you to do that.

Now, let me ask a couple of questions. I think fraud, waste, and abuse is appalling in any respect and I have seen it in my own private sector experience like the gentleman from California and I will get into that in a second. But let me ask you, Mr. Walker, to what extent—and Ms. Rivers touched on this a little bit about congressional add-ons, things in the Defense Department, things like helicopter carry ships and things like that—but let me ask this, to what extent does congressional action and inaction have impact on some of the issues you address in here and let me be specific.

You talked about EPA, the Department of Energy and others having trouble with Superfund collection of cleaning up sites. How much does the inaction of Congress, certainly since I have been here for 5 years and even 2 years prior to that, to pass any sort of Superfund reform legislation to try and cut through this mess have an impact on that? We, in fact, haven't even reauthorized the Superfund tax program, I think, for the last 4 years. What impact does that have?

And then let me ask you about things like the VA buildings. We heard about this a year or two ago. There were a number of press reports on this. But I think if I read correctly there was a great deal of congressional objection to closing down any VA buildings that might be in their district.

And then let me ask you about the FHA and the IRS. With the IRS there have been recent reports—a number of us pushed to bring Mr. Rossotti in, the man from the private sector to run the IRS, rather than having a tax lawyer in there running it—he has now raised concerns about the bill that I cosponsored and a number of us voted for, a Taxpayer Bill of Rights, saying that we now don't have sufficient auditors to enforce the Tax Code as it is. Are you finding problems in your work with that?

And then with respect to FHA and HUD, I was an investment banker back in the 1980s and 1990s before I came to Congress. And I did a transaction in Houston for a project, a multifamily project that had been FHA insured. We took it out of FHA. It was under the old coinsurance program. It was called, I think, Colonial Arms, if I recall correctly. It first was financed at \$35 million, if I recall; then it was refinanced at over \$40 million, when it was going belly up. And then it went belly up. My client bought the project at auction for \$7.6 million, as I recall, where it just barely cashed-flowed at those numbers and we privately financed it in the credit markets and the taxpayers took a bath for the rest.

That was under the old coinsurance program that HUD developed in the 1980s under Secretary Pierce, and if I recall correctly it wasn't until the latter part of the 1980s or early 1990s that Congress finally stepped in and eliminated that problem.

Now, with respect to FHA I have now heard two Secretaries of HUD testify before the Banking Committee about the need to reform FHA and restructure FHA much in the same way that the GSEs are, Fannie and Freddie, to give them more flexibility. Does your analysis indicate that if FHA was restructured along the lines that Secretary Cisneros originally proposed, give them more flexibility, that they would be able to address things like the lag time on REO and the impact on their cost, even though it is an overall profitable program. And I will stop there.

Mr. WALKER. Let me take a shot at trying to address some of those. First, with regard to the question of the Legislative Branch and what can the Legislative Branch do? First, I think more oversight which is what this hearing is intended to encourage. This is a beginning, not an end. There needs to be more oversight. Secondly, sometimes the Legislative Branch gets involved in micro-management and that has clearly happened in the case of Medicare. I mean it has prescribed solutions and it has prohibited HCFA from being able to exercise management responsibilities in certain areas where it makes sense.

With regard to VA, there is absolutely no question whatsoever they have significant excess capacity. The question is, how best to deal with that? And, therefore, should there be a civil base closing type commission or something. And it is not just VA. There is a lot of excess Federal facilities that don't have anything to do with DoD. The world has changed. Whether it be the State Department, whether it be the domestic agencies, we don't need to physically be everywhere that we had to be when we didn't have the type of communications and technology that we do today. And we ought to look at that especially with regard to costs, security threats, and other things.

Mr. BENTSEN. If I could just interject.

Mr. WALKER. Yes.

Mr. BENTSEN. FHA, as you know, on the Ginnie Mae program is going to a centralized function like Fannie and Freddie, which actually I have gotten complaints from some of the real estate industry about it. I think it is going to work out better and I think they will find that to be the case.

Mr. WALKER. With regard to Commissioner Rossotti, who I meet with every 3 to 4 months, because they have more than they can say grace over. We are trying to have a constructive engagement approach with them. And they do have an issue that the pendulum swung too far. The pendulum has swung too far in that they are very focused on customer service. They are not focused enough on compliance. There is a happy medium in there some place.

And, last, with regard to HUD, you know, additional flexibility may help but there are a lot of other things they need to do before you get to that point. I mean I think you need to make sure that they have got their priorities, they have got the people focused in the right area, they have got the right kind of controls in place and then at that point in time you might want to think about additional flexibility.

Mr. BENTSEN. And with respect to EPA and the Superfund?

Mr. WALKER. EPA and Superfund, Keith.

Mr. FULTZ. I would suggest that what EPA needs to work together with many of the other Federal agencies: they need to make better decisions on the basis of priority and risk-based decisions. We, as a nation, are facing cleanup costs in our Federal facilities that DOE, EPA and other Federal agencies manage approaching \$300 billion. And we are finding even within agencies, in fact, Mr. Spratt would be aware of the DOE problem, they have not prioritized, they have not identified and they haven't made risk-based decisions.

And what we mean is there are facilities that are being cleaned up today at tremendous cost that might not be at as much risk to the public safety and health as others. And these agencies need to do a much better job of making risk-based decisions.

Mr. BENTSEN. I am going to get gaveled on this but do you think the lack of—Congress has been talking about reforming the Superfund law for the last 6 or 8 years and every year we say, well, we can't get there—and do you think that has some impact on the agency's ability to carry out the law when they know that the sword of Congress is hanging above them on what the rules are going to be or what they ought to be doing?

Mr. FULTZ. I believe that the agency needs more direction and more guidance. And I think that would be helpful. They have administrative procedures which we recommended they need to improve upon, but clearly direction would be helpful.

Mr. BENTSEN. Thank you.

Mr. WALKER. But they can make some progress, too, without that direction.

Mr. BENTSEN. Thank you, Mr. Chairman.

Chairman KASICH. Mr. Hoekstra.

Mr. HOEKSTRA. Thank you, Mr. Chairman.

We just had a question as to—I can't read that chart and what is behind the trailer—but my question relates to in your testimony

on page five you identified Table I, which is the 1999 High-Risk Areas in the Year Designated. Does the Department of Education now fall under a high-risk area?

Mr. WALKER. There is one of the programs—the student loan program. It is just the program. It is not the entire department. Generally when we designate high-risk we designate it based on programs or functions, rather than a department.

Mr. HOEKSTRA. How can I get your attention on the Department of Education for an agency that gets \$35 to \$40 billion in discretionary funds, they manage a huge loan portfolio. For 1998 their books were not auditable or that they could not get a clean audit. We met with the auditors this week. They said that the grade for this year would possibly be a C— and perhaps as low as a D—, meaning that if they were a publicly held company the trading of their stock would be suspended or their market value would go down.

Yes, go ahead.

Mr. WALKER. First, we are not the auditors for the Department of Education. But there are some serious issues here that have to be addressed. They are one of the agencies that are lagging as far as the 24 major departments and agencies as it relates to financial management challenges and the ability to be able to get a clean opinion.

Jeff, do you have an opinion?

Mr. HOEKSTRA. They may be lagging and I know you are not the auditors.

Mr. WALKER. No.

Mr. HOEKSTRA. But reading the description of what you do is to following the Federal dollar and in this case we are running \$85 to \$100 billion through that agency and you can't follow the dollars.

Mr. WALKER. Well, let me address that directly for a second and then I will let Jeff comment. First, 95 percent of the work that GAO does is based upon congressional mandate, committee requests and member requests. So, we don't really have a whole lot of discretionary resources.

And, so, I am not exactly sure what we have going on right now in Education but Jeff might be able to tell us with regard to the financial side.

Mr. HOEKSTRA. And I think you have been helping us. And I think we are going to—well, Lorraine Lewis is going to be here—but I think also in the supplemental we are requesting a significant funding for either GAO or another entity to do a very in-depth analysis of what is going on within the Department because with that kind of money going through that Department and not having a clear flow or understanding where the money is going. So, what, you don't have the discretionary funds. It is our job to get you the discretionary funds to do a thorough analysis because if the books can't be audited you are just creating an environment that is ripe for waste, fraud, and abuse.

So, did you want to add something?

Mr. STEINHOFF. Yes. Basically this is an entity that just doesn't have the basic financial systems in place. They did get a clean audit opinion at one time but that was based on a heroic effort. It is my understanding Education prepared 1,800 spreadsheets, comb-

ing through records and coming up with numbers months after the year. Last year they issued their financial report, 8.5 months after the legislative due date of March 1.

They came out November 18. Education had a disclaimer of opinion, serious accounting problems, serious control problems. They are one of 21 of the 24 CFO Act agencies whose systems do not comply with the Federal Financial Management Improvement Act, an Act that was sponsored by one of your former colleagues, Senator and Representative Hank Brown.

Senator Brown knew the importance of getting to the end game of having the information day-to-day and having the systems and that is what they lack today.

Mr. HOEKSTRA. Good. Thank you.

Chairman KASICH. Mr. Moran.

Mr. MORAN. Thanks, Mr. Chairman. Actually, the Department of Education, and even I think the inspector general has another point on some of that I would say to my colleague, and most importantly some other facts that I think they will put on the record. I am not going to pursue it, but I think there is another very valid point of view on some of your major concerns there.

Mr. HOEKSTRA. They have had the opportunity to testify. And I think the IG agreed that books weren't auditable for 1998.

Mr. MORAN. Let me, I am not going to pursue that because we can get into it with the Education IG.

I have to say, Mr. Chairman, the worst things about waste, fraud and abuse is that it has been used as a sham by budgeteers for decades now. I think the first time was in 1971 when we used, as a plug figure, we put a billion dollars I think in as a line item in what was then an HEW budget because we didn't want to eliminate marginal programs, and we didn't want to say no to important constituency groups of program managers. And now the Appropriations Committee always does the Executive Branch one better and ups the figure. There is very little follow-up to see whether any of these estimates really have any substance to them.

And, generally, what does have substance to it are the kinds of managerial and programmatic reforms and changes that are necessary. The big-ticket items, of course, really, you have to look to the Defense Department, and I don't know whether Mr. Spratt agrees with me. I think theoretically he would, but if we really want to stay big bucks, we wouldn't have the Navy prepared for a land and air war, and we wouldn't have the Army prepared for a sea and air war, and the Air Force vice versa. There are a lot of traditional organizations that could be made more efficient, but there are a lot of reasons we don't do that.

Now that we have on-time delivery of inventory, you have to ask the question whether we need all of the supply people. Clearly, we don't. But the Congress is going to sustain them. And those are the kinds of programmatic and political decisions I think that are probably more relevant than some of the things that we try to do in the way of exposure of so-called fraud and abuse. It exists, but not anywhere near as much as we would like the people sometimes to believe.

There are some things though, specifically, that I want to ask you about. And at some point, I would really like a full investiga-

tion of the enormous amount of trucks, and tanks, and planes and even ships, although the ships aren't in the same location, that just sit out there rotting, thousands of them, particularly over in Europe, and I guess because we don't know what to do with them. But we could sell them to some countries that could use them, and they would hardly be threatening to our military forces. But I am going to ask the IG, Defense, about that.

What I am going to ask you about is a cross-cutting issue, and I want the Chairman to listen to this because this is something that is not going to come up. We went to the idea of credit card purchasing. Great idea. And you can do off-the-shelf purchasing, and you can use a Government credit card. But do you know that the credit cards are still charging 2 to 2.5 percent transaction fee when we purchase this stuff for the Government, even within Government sometimes? And we are paying, in some cases, millions of dollars for a transaction fee to a credit card company for a cost that is a few cents. It costs them a few cents. When you buy something for \$40 million, the transaction fee isn't any greater than it is if you buy something for \$4, and yet we are charging 2 percent of whatever that total amount is.

Now that is something that is a total waste. I think it is fraudulent, and yet we continue to do it because we won't stand up to Visa, and Mastercard and so on. And I would like to see if there has been any thought given to that and whether we might be able to—you know, that seems to be a pretty legitimate way to save some taxpayer dollars. Wouldn't you agree, Mr. Walker?

Mr. WALKER. It sounds like it is something that needs to be looked into and renegotiated. Let me also say for the record, Mr. Moran, I think as of Tuesday, I may become one of your constituents.

Mr. MORAN. Terrific. Well, that is the greatest, that is the best answer I could possibly have gotten, Mr. Walker. [Laughter.]

I think I have heard enough from this witness. He is a terrific witness. [Laughter.]

He is going to make a great constituent.

Chairman KASICH. Let me just pursue that a little bit. Are any of you aware of what my friend from Virginia is saying? I hope we are not giving them a piece of the action based on our—

Mr. WALKER. Well, we have not looked at it. I can, to my knowledge, I can follow up. But as you know, many times the way the credit card companies make money is they charge a percentage of the cost, and it ranges anywhere from less than 1 percent to American Express charges a lot higher.

One would think, with the volume that is commanded by the Federal Government, we ought to be able to get a pretty good deal. And, in fact, for things like telephone service and long distance service, we have gotten a great deal, and we are renegotiating about every other year to improve on that.

Jeff.

Mr. STEINHOFF. This is something we will look at much further. But I know that in some cases, like for the travel card, the Government earns money. We get a rebate.

Mr. MORAN. Travel card is different.

Mr. STEINHOFF. We get a rebate.

Mr. MORAN. Travel card you have done it. You have done what you need to do in the other areas. In some cases, where the, for example, technology services, which I am familiar with. We have got a lot of Government contractors. They are paying that kind of money for the supplies that they charge, but what they do is to just build it into the rates, and they charge the Government. So the taxpayer winds up paying it. They say it is a legitimate part of business, but it really is illegitimate for credit card companies not to give us a more reasonable rate, given the very high volumes of business. And the problem is they are a virtual monopoly now. They fix their interest costs, and we haven't stood up to them. It is something that I wish that the GAO would do, and I would really appreciate the comptroller general looking into it.

Chairman KASICH. Now, the gentleman is in the spirit of the thing. I appreciate the gentleman's comments.

I want to just conclude Mr. Walker's testimony. I, first of all, want to thank all of you. We have been meeting for a long period of time, my staff, along with the GAO staff, trying to get the right kind of research done. And then Mr. Walker and I had a chance to meet. I want to compliment you. I think you have done a great job. And I think it is not an easy job. And it is particularly not an easy job when you come up here.

And one of the guys here on the staff showed me this report that was done by John Conyers in 1992, "Managing the Federal Government: A Decade of Decline." And here we are in 2000, and you folks probably keep investigating. And then at some point, when you are not seeing anybody take it seriously, you say, why should I keep doing this? I mean, that is human nature.

I am going to get my old bill out on bounty hunters. I actually had a bill that passed the House a couple of times; in fact, Pat Schroeder passed it, that said—look, you can put anything in a law. They have got these performance programs in the Federal Government and these reward programs, but they are, in too many cases, in name alone.

And I have always believed that if you could document the savings of money, a million dollars, you ought to get a chunk of it as a Federal employee. And then you get into the problem of how do you determine it. But in the clear-cut cases, it would be terrific. I think the last thing that Federal employees want are more plaques. Give them the money. Show me the money, and I think we would have a lot more aggressive activity in the public sector to try to be more creative and imaginative.

But I want to thank you all. It is a hard job to be an investigator. And the only thing I can tell you is I don't want to contribute to the cynicism that there is another hearing on this, and we don't get anything done. I am going to do the best I can. And I am going to try to link up people who have a genuine interest. I mean, you have a person like Miller and a person like Bentsen who clearly have an interest in HUD and all of its attendant programs. You have got Mr. Hoekstra, who I think is a hero in what he has done in education, Jim. He really put his shoulder to the wheel, and he has really tried to be constructive in education. And we have got members here like Mac Thornberry, who are tremendously interested in Defense, along with a person like Mr. Shays.

We have a lot of people interested, and I just hope that we can create a mechanism where we can focus and try to accomplish a few things. If we can do that, then that will make your job more meaningful, and it will make your job more satisfying. And I just want you to know there are people here who care. And can we wipe it all out? I don't think so. But can we make more progress? I think the answer is that we can. And I don't believe the purpose of this is really to demagogue anybody. It is really designed to do what people expect us to do.

So I want to thank you for your testimony, Mr. Walker. I look forward to you perhaps even becoming part of our team here, that you can have some of your folks sit in with these task forces that we are most likely to create, and let us see what we can do. If we focus on five areas this year, I mean, narrow areas, and get something done, then it will have been positive.

So thank you for being here, and I would now like to have the four IGs come to the table.

Mr. WALKER. Thank you, Mr. Chairman.

Chairman KASICH. David, that was an excellent job. You did an excellent job of testifying too. Thank you.

We are now going to hear from four IGs. We are going to hear from June Gibbs.

If you would quickly take your seat. We are going to hear from June Gibbs Brown, who is the inspector general at HHS; Mr. Donald Mancuso—is it “cuso” or “cooso”? I had a second grade teacher—

Mr. MANCUSO. Mancuso, Mr. Chairman.

Chairman KASICH. Wonderful. Wonderful.—who is the deputy inspector general at the Department of Defense. We are also going to hear from Susan Gaffney, who is the IG with HUD, who we have already heard a little bit from and from Lorraine Pratt Lewis, who is at the Department of Education.

I think what we ought to do is—now, when I look at this panel, and I see three women and one man, since I now have two little girls, there is a future in this business for them; is that correct? [Laughter.]

OK. I like to see that. Anyway, why don't we start, any idea how you want to—have you talked among yourselves? Probably not. Why don't we start with Mrs. Lewis and work left to right.

Here is what I would like. I hate to have you summarize, but you are going to have to. But I also would like to have the IGs involved with whatever mechanism we create here. We do not want you cut out of this business either, and I assume you have staff people that work underneath you. And let us just get a little life in all of this stuff and see where we are, but we want to have you included, just like we did the GAO.

**STATEMENTS OF LORRAINE LEWIS, INSPECTOR GENERAL,
U.S. DEPARTMENT OF EDUCATION; SUSAN GAFFNEY, IN-
SPECTOR GENERAL, U.S. DEPARTMENT OF HOUSING AND
URBAN DEVELOPMENT; DONALD MANCUSO, DEPUTY IN-
SPECTOR GENERAL, U.S. DEPARTMENT OF DEFENSE; AND
JUNE GIBBS BROWN, INSPECTOR GENERAL, U.S. DEPART-
MENT OF HEALTH AND HUMAN SERVICES**

STATEMENT OF LORRAINE LEWIS

Ms. LEWIS. Thank you, Mr. Chairman, Mr. Spratt. Good to see you again Mr. Hoekstra. I do have a longer statement for the record, which I offer.

I will be discussing a few of the management challenges that we identified in the letter to you and several other members and Senators last December. Of course, a top priority for the Department is its preparation and access to accurate financial data. This information is critical for the Department to make informed decisions, manage for results and ensure the integrity of its operations.

Due to weaknesses in the Department's financial system, the work performed on the fiscal year 1998 statements resulted in reports containing disclaimers of opinion. The work on the fiscal year 1999 departmentwide and SFA statements is continuing. It appears at this point that the audit reports will contain four qualified opinions and one disclaimer of opinion.

There are many internal control weaknesses that were reported in fiscal year 1998 and continue to be reported in fiscal year 1999. However, the Department has developed processes and utilized contractors to work around the underlying systemic problems. As a result, the Department was able to prepare this—

Chairman KASICH. Could I just ask you a question?

Ms. LEWIS. Yes.

Chairman KASICH. You are a very knowledgeable person, right? Why don't you just tell us. I mean, if you want to read through that, that is fine. But if you want to say, "Here, is what I am kind of thinking about all of this."

Ms. LEWIS. All right.

Chairman KASICH. Just be casual about it.

Ms. LEWIS. We will be reporting on or before March 1st, which is the deadline, on the fiscal year 1999 statements. They do show improvement for the Department. This is the very first year that the Student Financial Assistance Office audit will be conducted. Again, both audits at this point will appear to show four qualified opinions and one disclaimer of opinion. This, I believe, is the result of much dedicated work on the part of the Department officials, the OIG auditors and, of course, our independent professional contractor Ernst & Young.

Indeed, as you have previously noted, underreporting of income by applicants for student aid and their parents remains a problem. We believe this is a problem that costs the taxpayers about \$100 million or more each year. There was discussion previously about the law 2 years ago, the amendment to the Higher Education Act, which authorized the Secretary, in consulting with the Treasury Department, to engage in a match, a full-scale data match. It is, indeed, the case that this match has not been implemented. There

are continuing discussions. It is my understanding, between OMB, Treasury, and the IRS and the Education Department about this matter, that the nominee for the Treasury Secretary, Mr. Summers, indicated previously that the IRS's legal opinion is that that law which amended an Education Act did not provide sufficient authorization for the IRS to provide this data to the Department of Education without the individual's consent.

We know the Treasury Department is doing a review of that particular section, 6103 of the Internal Revenue Code, which I believe is a report that is being mandated by Congress, and that report may show their current thinking. Our position is, if it does require additional legislative amendment in the Title 26, we would hope that that could be accomplished quickly. We view this as a front-end fix to a very serious problem, which will create efficiencies throughout the system in the long run.

Another report the IG Office has issued recently related to the inappropriate death and disability discharges from student loans. My longer statement refers to some of the numbers that we found there. We did make some key recommendations to the Department. In fact, it was the Department who asked us for this audit because they saw a rise in these discharges. And we did report on that in June of 1999.

The Department has issued guidance to the guarantee agencies in terms of fixes. It now requires an original or a certified copy of a death certificate in an application for a discharge for death. And also on the disability side, it requires the doctor to identify his or her State license number, as well as a telephone number and provides additional information on what the guarantee agencies can do to tighten up this system.

I identified a number of other areas in my longer statement, and in the letter I referred to earlier, and I would be happy to discuss any and all of those issues.

Thank you.

[The prepared statement of Lorraine Lewis follows:]

PREPARED STATEMENT OF HON. LORRAINE LEWIS, INSPECTOR GENERAL, U.S.
DEPARTMENT OF EDUCATION

Good morning Mr. Chairman and members of the Committee. I am pleased to testify before the Committee on the Budget on matters relating to management challenges at the Department of Education.

On December 8, 1999, we provided to Congress an assessment of the Department's significant management challenges. Many of these challenges concern long-term issues that we are continuing to monitor. The December 8 letter describes the work the Department is doing, or needs to do, to meet these challenges. I have attached a copy of the December 8 letter for the record.

FINANCIAL MANAGEMENT AND INTERNAL CONTROLS

A top priority for the Department, and one of its most significant challenges, is its preparation of and access to accurate financial data. This information is critical for the Department to make informed decisions, manage for results and ensure the integrity of its operations. It is an area identified by the Department as a material weakness in its fiscal year (FY) 1999 Federal Managers' Financial Integrity Act (FMFIA) report.

Due to weaknesses in the Department's financial system, the work performed on the Department's FY 1998 financial statements resulted in reports containing disclaimers of opinion. The work on the FY 1999 Department-wide and Student Financial Assistance (SFA) financial statements is continuing, but it appears that the audit reports will contain four qualified opinions and one disclaimer of opinion.

Although significant internal control weaknesses carried over from FY 1998, and will continue to be reported for FY 1999, the Department has developed processes and utilized contractor support to work around the underlying systemic problems. As a result, the Department was able to prepare financial statements in a more timely manner and provide sufficient support for amounts shown. This enabled the auditors to complete their audit and render a qualified opinion on four statements, but a disclaimer of opinion on the Department's and SFA's Statement of Financing.

One of the significant weaknesses in its financial reporting process relates to the Department's general ledger software package. To address this issue, the Department is in the process of procuring a new general ledger system intended to overcome many of the system weaknesses preventing the preparation of timely financial statements. However, until its new accounting system is operational, the Department will have to continue its work around procedures.

During FY 1998 and again in FY 1999, the Department's reconciliation procedures were not performed on a timely basis. In addition, the identified reconciliation differences were not always adequately explained, resolved and posted to the Department's general ledger. Weaknesses in the Department's internal controls over the reconciliation process prevented timely detection and correction of errors in its underlying accounting records. Despite these underlying control weaknesses, the auditors were able to conduct sufficient tests of balances and transactions to enable them to express a qualified opinion on four of the financial statements. The Department is in the process of implementing new automated procedures to assist in the cash reconciliation process and the reconciliation of other internal accounting records. The Department also is performing more timely reconciliations of its fund balance with Treasury.

When I testified before the Subcommittee on Oversight and Investigations, Committee on Education and the Workforce on December 6, 1999, I stated that we would issue the audit reports for the FY 1999 financial statements of the Department and SFA by March 1, 2000. I still plan to meet my commitment. We will continue to work with the Department and Congress to improve the Department's financial management.

IRS DATA MATCH AND DISCHARGE OF STUDENT LOANS

Another management challenge that we have identified is the under-reporting of income by applicants for student aid (and their parents). Our audit and investigative work has shown this is a problem that is costing Federal taxpayers over a hundred million dollars annually in overawards of Pell Grants and awards to ineligible persons.

In a 1997 audit report, we found that 3.7 million out of 9.1 million applicants for Federal student aid received Pell Grants during the 1995-96 award year. For 2.3 million of these applicants, we verified the adjusted gross income they reported on their financial aid applications with income data maintained by the Internal Revenue Service (IRS). Out of this sample, we reported that 102,000 students received Pell Grant overawards totaling approximately \$109 million. This is a conservative amount because we were unable to verify the reported income of parents of dependent students.

As recommended by our office, and supported by the Department, the Higher Education Act (HEA) Amendments of 1998 included a provision authorizing the Department, in cooperation with Treasury, to confirm with the IRS the adjusted gross income, Federal income taxes paid, filing status and exemptions reported by applicants (including parents) on their Federal income tax returns for the purpose of verifying the information reported on their student financial aid applications.

Currently, the Department is discussing the development of a test match study with the IRS. The Department has indicated that it will send samples of student aid applicant data to the IRS in March and June 2000. The IRS will match these data against its records and provide the Department with statistical summaries evaluating the accuracy of the applicant data.

It is our understanding that the Department will use the statistical information provided by the IRS to identify the types of students who are most likely to under-report their income. The Department intends to use the information to better focus their selection of student applicants for income verification at the school level. The Department also intends to use the IRS information to better evaluate the extent of income under-reporting and use the data in support of its continuing effort to conduct a full-scale data match with the IRS.

Although the HEA authorizes the Department to confirm student applicant income with the IRS, the IRS has indicated that it cannot disclose this information to the Department because such release is not authorized by the Internal Revenue

Code. Without specific authorization in the Code, the IRS indicates that it must obtain written taxpayer consent before individual income information may be released to the Department. In an attempt to overcome these obstacles to full-scale verification, the Department, Treasury and OMB are working together to develop possible solutions, including legislative and administrative changes.

Another concern in the SFA area is the inappropriate discharge of student loans based on disability or death. The HEA provides for the discharge of a student loan when the borrower becomes either totally and permanently disabled or dies.

At the request of the Department, we conducted an audit of the Department's controls over the discharge of student loans due to disability or death. In June 1999, we reported that borrowers who received disability discharges of over \$73 million were earning wages and borrowers who received disability discharges of nearly \$11.5 million returned to school and received additional loans and grants. Additionally, our review identified over \$3.8 million in loans discharged for borrowers who inappropriately received a death discharge.

To help correct this abuse, we recommended that the Department take several steps to enhance the current discharge determination procedures, including revising the disability form to include, at a minimum, the doctor's professional license number and office telephone number and requiring certified copies of death certificates. In response, the Department modified its disability form to incorporate our recommendations and OMB approved the form. In addition, the Department now requires that a death discharge be based only on an original or certified copy of the death certificate.

Our office continues to pursue this matter and we are engaged in a project to identify fraudulent disability and death loan discharges. In order to identify fraudulent death discharges, we conducted a data match with the Social Security Administration's Death Index to determine persons who received loan discharges based upon death but who do not appear in the Social Security records. Working with a sample of these data and with information filed by those who obtained substantial discharges from Sallie Mae and a guaranty agency, our investigators are pursuing initial leads generated by the match. We intend to continue this effort as more of the match data are analyzed. In the area of disability discharge fraud, we are working with a number of guaranty agencies to identify potential fraud cases and following up on leads developed from the data. These projects involve coordination with a number of other entities, including the Department's program office, guaranty agencies, state agencies and Sallie Mae.

The OIG also is investigating a number of individuals for disability and death discharge fraud. In one completed case, a defendant was recently prosecuted and sentenced for obtaining the discharge of five loans totaling \$37,000, based upon false claims of disability for mental illness. Two other indictments for false claims of disability also are pending in OIG cases. In addition, our investigative efforts to date have led to the reinstatement of over \$560,000 in student loans for borrowers who falsely claimed to be totally and permanently disabled.

INFORMATION SYSTEMS AND SECURITY CONTROLS

The Department has been successful in its efforts to ensure its programs are Year 2000 (Y2K) compliant. This success was accomplished through a concentrated effort on the part of the Department, including technical assistance from our office. We contributed to the Department's success by evaluating its progress, identifying high-risk areas and providing information on the status of its major trading partners. The Department's commitment resulted in there being no interruption in its customer service and no loss of critical data from its computer systems. We would like to see the Department undertake a similar initiative in the area of security controls.

In December 1999, we issued a draft audit report on the Department's security policies and plans for its 14 mission-critical systems. The 14 systems include 11 SFA systems; the Department's Central Automated Processing System (EDCAPS); the Department-wide network (EDNET); and the Impact Aid System. Our review revealed that the Department has significant control weaknesses including a lack of security plans and reviews for six mission-critical systems, no process to ensure resolution of identified security deficiencies and a lack of technical security training for many employees responsible for overseeing the Department's computer security. The Department has informed us that it concurs with our findings.

Our draft findings indicate a weakness in the Department's compliance with the security requirements of the Computer Security Act, Paperwork Reduction Act and OMB Circular A-130. The Department also identifies this area as a material weakness in its FY 1999 FMFIA report. Currently, we are conducting a follow-up audit to determine the adequacy of security reviews performed on eight mission-critical

systems to meet OMB A-130 requirements. Additionally, we are evaluating the public, internal and privileged access vulnerabilities of the Department's EDNET communication infrastructure. We plan additional reviews of security controls for other systems in the future.

We also are participating with 16 Federal agencies in a President's Council on Integrity and Efficiency (PCIE) effort to evaluate compliance with Presidential Decision Directive (PDD) 63. PDD 63 calls for a national effort to ensure the security of the interconnected infrastructures of the United States. Our work focuses on the Department's efforts to comply with the requirements of PDD 63. Additionally, we have initiated an audit of the Department's disaster recovery planning for its mission-critical systems.

In another information systems area, the Department continues to explore ways to make its SFA program delivery systems electronic and paperless. The Department's goal of paperless systems creates new opportunities for efficiency, but requires effective controls to ensure accountability, security and legal enforcement. A particular challenge is the implementation of an electronic signature validation process that meets the requirements of OMB's implementation guidance for the Government Paperwork Elimination Act, which is expected to be released in April 2000. To assist the Department, we will provide advice to SFA on its current implementation of Personal Identification Numbers (PINs) in its financial aid application process. Additionally, we are researching the major components within a well-controlled Public Key Infrastructure (PKI) environment to assist the Department in its future PKI implementation efforts.

The Department also is working to implement three key requirements of the Clinger-Cohen Act, which requires agencies to improve management of information technology. These requirements include the implementation of a capital planning and investment control process, development of a sound and integrated information technology architecture and an assessment of the information resource management knowledge and skills of agency personnel. Although the Department has not fully implemented the requirements of the Act, it is making progress in addressing recommendations made by our office. The Department recently produced a draft Capital Planning and Investment Control Program and is working with a contractor to complete an information technology architecture. The Department also is working to complete a skills inventory to assess the existing skills of its information technology employees.

RESULTS ACT

The Department's first performance report, required by the Government Performance and Results Act, is due in March 2000. The Results Act reporting requirement presents significant challenges for the Department. These challenges include the supplemental funding role of the Department, relative to state and local government entities, in many education programs; the heavy dependence on third parties such as lenders, guaranty agencies and state and local education agencies to provide performance data; and priorities that compete with data collection such as the desire to reduce regulatory burden and increase flexibility in program implementation. These conditions will present ongoing challenges for the Department in its data collection and reporting efforts.

In a September 1998 audit report assessing the Department's implementation of the Results Act, we recommended that the Department establish controls over the analysis and reporting of data, establish standards for reporting performance information and establish a formal system for tracking indicators. Last year, the Department developed draft data quality standards and conducted training on these standards. The Department also plans to develop an electronic system for indicator tracking.

At the request of the Department, we also reviewed the processes used by State Education Agencies (SEAs) to collect and report data to the Department. Our review focused on two of the Department's major state formula grant programs—the Elementary and Secondary Education Act Title I Program and the Perkins Vocational and Technical Education Program.

Our January 2000 draft report documented the challenges of collecting and processing required student data and provided insight into state quality control procedures. We reported that the SEA process of collecting data for the two formula grant programs is complex because of the thousands of entities providing data. Each SEA also has its own unique control structure and processes for the collection of data.

To address the complexities of the data collecting and reporting process under the Results Act, the Department is working with states to reduce paperwork and to streamline the Federal education program reporting system. The Department also

is developing a pilot project called the Integrated Performance and Benchmarking System, which is designed to be an Internet-based system for harvesting data from states about Federal program activities at the school and district level. The Department is working with the Council of Chief State School Officers on this project.

We will continue to assist the Department in its effort to improve data quality under the Results Act. During the development of its Strategic Plan, the Department agreed with our recommendation to include in its performance report an assertion from Department program managers regarding the reliability and validity of the data used for performance measurement. The impact of this assertion requirement will be addressed in the Department's upcoming performance report. We also have been conducting a continuing assessment of the Department's selection of performance indicators and its reporting process. Based on this assessment and our review of the Department's first report, we will provide the Department with recommendations for improvement for the next reporting cycle.

COMPLIANCE MONITORING

With the increasing emphasis on accountability for results, it is important to consider the implications of this change on program oversight for the Department, State Education Agencies (SEAs), local educational agencies (LEAs) and schools. Program oversight is essential in the enforcement of program requirements, the development of necessary program guidance and the evaluation of program modifications during the legislative reauthorization process.

In a February 1999 report, we recommended that the Department assume a greater role in ensuring elementary and secondary program integrity. Specifically, we recommended that the Department integrate on-site program reviews, audits, technical assistance, reporting and evaluative studies. We also recommended that the Department's oversight consider SEA analyses of LEA single audit findings and emphasize corrective action follow-up.

With the increasing delegation of elementary and secondary program oversight to SEAs and LEAs, our report also recommended that the Department establish minimum standards for SEAs in monitoring the LEA administration of these programs. Our recommended standards included a requirement for SEAs to systematically analyze the results of LEA audits and other oversight activities to identify trends in findings and develop monitoring and technical assistance strategies to reduce occurrences of similar problems.

The Department has taken steps to address some of these oversight concerns. The Office of Elementary and Secondary Education has established integrated review teams to perform coordinated, multi-program reviews of the implementation of Federal education programs by SEAs. The Department also included in its proposal for reauthorizing the Elementary and Secondary Education Act a section under Title XI that addresses state requirements for monitoring LEA compliance with the Act. In addition, our office is participating with the Department in a pilot program with four SEAs that will address the better use of LEA single audits for targeting monitoring and technical assistance activities.

We are conducting additional reviews of compliance monitoring in elementary and secondary programs. We are completing an audit to determine whether the Higher Education Act Title III program is being monitored in an efficient and effective manner and whether adequate enforcement action is being taken by the program office. Another audit will evaluate the Department's monitoring of elementary and secondary formula grant programs.

We also will continue our work with the Department on the K-12 Auditing, Monitoring and Technical Assistance Support Project to develop an internal data exchange system to improve the Department's program monitoring process.

At this time, I would be pleased to answer any questions you may have.

Chairman KASICH. Ms. Gaffney.

STATEMENT OF SUSAN GAFFNEY

Ms. GAFFNEY. Mr. Chairman, Mr. Spratt, members.

When you are at HUD trying to minimize fraud, waste and abuse, you are highly motivated to do so for a couple of reasons:

One, HUD is serving only about one out of five of the households in this country who are eligible for HUD assistance. So every dollar we are losing to waste, fraud and abuse is a dollar some needy household is not getting.

The other thing that gets to you about HUD is that fraud, waste and abuse in HUD tends to be manifested in really abysmal living conditions. We pay an enormous amount of money because of fraud, waste and abuse to house needy people in terrible conditions, and no one wants that. It gets you motivated.

Mr. Chairman, and particularly, Mr. Spratt, this has been a very thoughtful discussion today. The point of my written testimony and perhaps it wasn't clear, was to say there hasn't been much thoughtful discussion about waste, fraud and abuse in this Government. What I see having happened over the last years has been very superficial. There has been some kind of an assumption that if you downsize the Federal bureaucracy, that is wonderful. You have won the war against waste, fraud and abuse. If you contract out, that is good, that is wonderful in and of itself. If you get an unqualified audit opinion, people seem to think that means you have solved all of your financial problems.

None of these things should be taken, in and of themselves, or even collectively, as giving you an adequate basis for assessing fraud, waste and abuse. I don't think GPRA is going to do that either. I don't think there are any silver bullets in this area. I think what it takes is oversight, oversight, oversight, and I should tell you, from my experience, oversight is not there on either the congressional side or the Executive Branch side. Fighting fraud, waste, and abuse also requires legislative reform. The Comptroller General was incorrect about HUD when he said that there had been legislation to consolidate/streamline HUD programs. There has not been. The number of programs has continued to grow. There is no attempt to match the programs with the capacity of the staff to manage them. And if it is not clear, I am blaming the Congress here. Maybe the Administration has some part in it, but this is what the Congress is supposed to be doing.

Now, I would like to make a couple of remarks about HUD 2020. First, HUD is inherently vulnerable, is inherently high risk, and that is because we have half a trillion dollars of mortgage insurance in place, we have 3,400 housing authorities, we have 4.4 million households who are receiving assistance.

The second thing nobody talks about, but I would like to talk about, is another reason why HUD is vulnerable. Every one of these well-meaning programs seems to generate an industry that grows up around it, and that industry ends up knowing the programs and the loopholes in those programs better than the HUD people know them.

The third thing about management reform at HUD is that the management reform agenda changes with each Secretary. The entire bureaucracy in HUD engages in each of these changed agenda. It is not as though there is a civil service standing to the side, tending to the institutional needs of HUD, no. Every 4 years, every 2 years, every 18 months, whatever it is, there is a new reform agenda. So my plea to you is: HUD has downsized so severely, we are embarked now on this HUD 2020 Management Reform, and I don't think there is any way to go back; we must go forward. I plead with you to take a role in making sure that it actually works, that it continues; that, for instance, the whole thing doesn't fall

apart when Secretary Cuomo leaves office because it is associated as his management reform plan.

That concludes my testimony.

[The prepared statement of Susan Gaffney follows:]

PREPARED STATEMENT OF HON. SUSAN GAFFNEY, INSPECTOR GENERAL, U.S.
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Chairman Kasich, Ranking Member Spratt, and members of the Budget Committee, I appreciate the opportunity to appear before you today to give you my perspectives on waste, fraud, and abuse in the Federal Government.

My perspectives are based on the 6½ years I have spent as Inspector General (IG) at the Department of Housing and Urban Development (HUD). IGs, as you well know, are required by statute to focus on promoting economy and efficiency, and preventing and detecting waste, fraud, and abuse. I think it's fair to say that, as a result of their very focused mission, the IGs have developed considerable expertise in these areas. That, of course, does not mean that the IG view is the only view to consider in evaluating Federal programs.

It's also important to keep in mind that I am the IG at HUD. I work at HUD, and so do the other people in the HUD OIG, because we believe in HUD's core mission. We are committed to fighting waste, fraud, and abuse in HUD programs and operations because every dollar lost to such activities is a dollar that people who need HUD's assistance aren't getting. Despite a robust economy, HUD serves only about one fifth of those households that could qualify for housing assistance. It's also easy to get motivated to fight waste, fraud, and abuse when the results of such activities are graphically manifested in the form of deplorable living conditions.

I do not see waste, fraud, and abuse as a political issue, but I think that others might. There is, for instance, concern that acknowledging waste, fraud, and abuse will lead to the demise of needed programs. Accordingly, there is a tendency to declare that the battle against waste, fraud, and abuse has been won. There is also the fact that fixing the problems that lead to waste, fraud, and abuse tends to require either sustained concentration on boring, bureaucratic processes, and/or changes in programs that have established constituencies. As a result of these factors, it seems to me that the discussion about, understanding of, and perhaps concern about waste, fraud, and abuse in the Federal Government are quite shallow.

Take the case of HUD. When Secretary Cuomo took office in January 1997, he said that HUD had become the poster child for mismanagement, and he vowed to turn the Department around. And indeed, over the past couple of years, Secretary Cuomo has reported a reinvigorated, more efficient, and more effective HUD. These reports have largely been based on HUD's getting a "clean" audit opinion on its financial statements; the Secretary's downsizing of the HUD bureaucracy; the proclaimed success of Secretary Cuomo's HUD 2020 Management Reform; Secretary Cuomo's launching of new programs; positive assessments by consultants paid by HUD; and increased appropriations for HUD. Permit me to look at each of these measures of success from an IG's perspective.

IS HUD'S "CLEAN" AUDIT OPINION A SUCCESS STORY?

In March 1999, the OIG issued its audit of HUD's 1998 financial statements. For the first time ever, HUD received an unqualified opinion, meaning that HUD had produced complete and reliable financial statements. The unqualified opinion got good press, and Secretary Cuomo threw a celebration party for HUD employees. The Deputy Director of OMB and "Mr. Clean" attended.

There are two big problems with this apparent success story.

First, HUD paid a contractor more than \$2 million to get its 1998 financial statements in the shape required for an unqualified opinion. This is problematic for a variety of reasons. Obviously, it's a lot of money to spend to get an unqualified opinion for a governmental entity; that amount of money could have provided housing assistance to about 350 needy households. Further, it shouldn't have been necessary—HUD's financial management systems should be able to produce the financial statements without further, extensive work. But, if the financial management systems aren't up to the task, and they aren't, then we cannot assume that HUD will continue to get unqualified opinions—unless they pay for the additional contractor work each year. This year, a similar contract is in place to put the financial records in order.

Second, the clean or unqualified opinion was equivalent to the OIG's saying that HUD had a balanced checkbook. The more important question is whether the money was spent for the right purposes. This question was addressed in the Report on In-

ternal Controls, which accompanied the audit opinion and listed eight material weaknesses. The material weaknesses may sound like “green eye shades” types of concerns, but they actually constitute serious deficiencies in HUD’s ability to ensure that funds are spent for proper purposes. The eight material weaknesses are:

- HUD needs to do more to ensure that subsidies are based on correct tenant income.
- Improvements are needed in multifamily project monitoring.
- HUD needs to complete improvements to its financial management systems.
- HUD must improve the management of its resources.
- Monitoring of insured mortgages needs to place more emphasis on early warning and loss prevention.
- The Federal Housing Administration (FHA) needs to improve its accounting and financial management systems.
- HUD must address problems that cause resource shortages affecting FHA programs.
- FHA must improve Federal basis and budgetary accounting.

Consider the import of the first material weakness, which is gently labeled “HUD needs to do more to ensure that subsidies are based on correct tenant income.” This material weakness has its foundation in an estimate that in 1998, under its public housing and Section 8 programs, HUD made housing subsidy overpayments totaling \$857 million (as compared to total spending under these programs of \$15.5 billion). HUD made the overpayments because some recipients underreported or didn’t report their true incomes; and neither HUD nor the administering housing authorities had control systems adequate to identify the underreporting or failure to report. This matters a lot, because, again, every dollar of overpayment is a dollar that is not being made available for truly needy families who are on long waiting lists for HUD assistance.

HUD acknowledges this weakness and intends to correct it through a process that starts with matching reported tenant incomes with IRS and Social Security income data. HUD’s first match of data (for calendar year 1998) identified 280,000 instances of income underreporting that exceeded established thresholds (\$4,000 for project-based Section 8; \$8,000 for public housing and tenant-based Section 8). This week, HUD started mailing letters to tenants asking them to explain the discrepancies to the PHAs or owners. HUD will also be notifying the PHAs or owners that discrepancies exist and providing them with instructions to remedy the discrepancies and report back to HUD. Since this methodology has not yet been tested, and there is question about the accuracy of the tenant income data in HUD systems, we are concerned that a large number of tenants may receive erroneous income discrepancy letters (for calendar year 1998 income), which will have negative long-term implications for the computer matching program.

Or consider the second material weakness, “Improvements are needed in multifamily project monitoring.” This material weakness concerns HUD’s oversight of about 30,000 privately and non-profit owned multifamily projects. The Report on Internal Controls says that:

“Overall, we found that monitoring of troubled and potentially troubled assisted projects was inadequate. We noted audited financial statements that were not submitted and reviewed, and physical inspections and management or occupancy reviews that were not performed by the field offices. In addition, field offices were not adequately following up to resolve identified deficiencies.”

This material weakness was first reported in the financial audit for Fiscal Year 1991. HUD’s compliance and monitoring approaches for dealing with problem multifamily projects are still evolving.

You might be asking, “So what?” Results from the OIG’s Operation Safe Home multifamily equity skimming initiative are instructive. Equity skimming is the misuse, by an owner or managing agent, of any part of the rents, assets, proceeds, income or other funds derived from an FHA insured multifamily project, in violation of the Regulatory Agreement between the owner and HUD. Mortgage defaults and deteriorated living conditions tend to go hand in hand with equity skimming. So, in 1994, the OIG made it a priority to identify equity skimming and get diverted funds repaid or the projects repaired. Between 1994 and September 30, 1999, we examined 147 multifamily projects and then, in conjunction with HUD and the Department of Justice, successfully pursued repayments of more than \$90 million.

The OIG is maintaining its focus on equity skimming:

- Last month, for example, based on a lengthy investigation by the OIG and the FBI, the U.S. Attorney for the Middle District of Florida announced guilty pleas by 10 individuals and one business. They had conspired in an equity skimming scheme which allowed the owners of 13 HUD-insured multifamily developments to illegally divert more than \$987,000 between 1991 and April 1995.

- Last week, based on another lengthy investigation by the OIG and the FBI, the U.S. Attorney for the Northern District of California announced the indictment of a prominent figure in the multifamily industry on 19 charges of stealing over \$1.8 million from multifamily projects, defrauding the United States and HUD, and paying illegal kickbacks. The grand jury, which expressed outrage that HUD hadn't detected and stopped these practices, gave a standing ovation to the auditors and agents who had conducted the investigation.

HUD officials have acknowledged that corrective action is needed in these eight areas of material weakness. The unqualified opinion does not justify overlooking the fact that these long-standing, serious problems continue to exist.

SHOULD THE DOWNSIZING OF HUD BE CONSIDERED A SUCCESS STORY?

Efforts to reduce the Federal bureaucracy seem to be universally applauded, and Secretary Cuomo has in fact claimed HUD's downsizing as a major accomplishment.

I am somewhat perplexed by this tendency to see downsizing, in and of itself, as a good thing, without regard to the bigger picture of overall expenditures and impact on program delivery. At HUD, there is evidence that the downsizing that started in 1995 has increased costs as well as program abuse.

In June 1995, as part of his "Response to GOP Proposal to Dismantle HUD," Secretary Cisneros issued a Reinvention Blueprint that called for a radical restructuring of HUD programs and the "transformation of HUD from a lumbering bureaucracy to a streamlined partner with State and local governments. Significant downsizing is anticipated, reducing HUD's current workforce of 12,000 today to fewer than 7,500 employees." There was no analytic basis for the 7,500 target. Further, the radical restructuring of HUD programs was subsequently shelved, but HUD's commitment to downsizing continued through rounds of untargeted buyouts.

By the time Secretary Cuomo took office in January 1997, HUD's staffing had been reduced to about 10,500. Secretary Cuomo announced his commitment to achieving the target staffing level of 7,500; and, a little more than a year later, HUD staffing was at 9,100, the reduction once again having been accomplished through use of untargeted buyouts. After massive staff reshuffling among programs and locations, however, it was the Single Family Mortgage Insurance Program that took the brunt of the staffing reductions; its staff was cut in half.

The Secretary's HUD 2020 Reform Plan envisioned contracting out as a principal means of compensating for the Single Family staff reductions. Notably, HUD's Real Estate Owned (REO) single family properties (acquired as a result of HUD's paying insurance claims) would be managed, marketed, and sold by a few full-service contractors, as opposed to those functions being handled by a combination of HUD staff and about 350 real estate asset management contractors. The new management and marketing contractors were to be in operation by October 1998.

HUD never analyzed the costs and benefits of this approach. When OIG auditors questioned why program officials hadn't prepared the cost comparison required by OMB Circular A-76, program officials answered that they weren't required to, because the new contracting wouldn't affect the jobs of more than 10 employees. That's because the aforementioned staffing reductions had already taken place.

So what? Well, the major staffing reductions took place in the fall of 1997. Because large scale procurement isn't one of HUD's strongest suits, the new management and marketing contractors didn't start operation until April 1999 (rather than October 1998, as planned). In the intervening 15 months, OIG auditors found that "inventory increased, sales to homeowners declined, age and condition of FHA properties deteriorated, revenue was lost, and holding costs increased. * * * FHA management issued emergency contracts, and placed temporary, inexperienced, and/or untrained HUD staff in property disposition jobs. The effort did not overcome the problems."

HUD awarded 16 management and marketing contracts having an estimated 5-year cost of \$927 million. Seven of these contracts (with an estimated 5-year cost of \$367 million) were awarded to a single contractor, Intown Management Group. OIG auditors looked for but couldn't find any evidence that HUD officials had assessed Intown Management Group's financial capability to handle this huge workload (estimated to be 40 percent of HUD's total REO inventory). Forty-five days into the contract period, Intown voluntarily withdrew from one of its seven contracts. Six months into the contract period, HUD terminated Intown's six other contracts for non-performance. At that time, Intown had sold only about 2.8 percent of its assigned inventory.

By the end of January 2000, HUD's REO inventory totaled 47,711 properties, 42 percent of which had been in the inventory 6 months or more, and 17 percent of which had been in the inventory 12 months or more. Ten months earlier, when the

management and marketing contractors started work, the inventory had totaled 43,560 properties, 30 percent of which had been in the inventory 6 months or more, and 10 percent of which had been in the inventory 12 months or more. These statistics demonstrate the difficulty of disposing of properties that have been in the inventory for long periods and the tendency of contractors to focus their efforts on disposing of recently acquired properties.

This matters a lot. Vacant, boarded up HUD-owned homes have a negative effect on neighborhoods, and the negative effect magnifies the longer the properties remain in HUD's inventory. The good news part of this sad saga: the neighbors throughout the country have made their anger about the HUD REO situation known to the media and the Congress.

The downsizing of the Single Family staff has also afforded increased opportunities for fraud. For example:

- OIG and FBI investigation established that Allstate Mortgage Insurance, a HUD-approved lender in the Direct Endorsement Program, originated more than \$97 million in 427 fraudulent loans during the period June 1996 through July 1997. OIG auditors followed up to find out why Single Family staff had not detected a fraud of this scale. The auditors concluded that staffing reductions had eroded the Single Family staff's ability to adequately oversee mortgagees' loan origination practices, a situation that was exacerbated by confusion about a new HUD 2020 policy designed to compensate for the staff reductions.

- In January 2000, as a result of another OIG and FBI investigation, a HUD Housing Specialist in the Los Angeles Office pled guilty to receiving \$80,000 in kickbacks in exchange for selling about \$2.1 million in HUD REO properties to a real estate company owner for only about \$700,000. OIG auditors again followed up to find out why HUD staff had not detected this fraud, which continued over a 7-month period. They found that the Housing Specialist's work had been subject to no supervisory review. The responsible supervisor said the office's REO workload was too large, and the pressures to dispose of it too great, to allow for any supervisory review.

I trust that this recounting explains why I do not believe that downsizing, in and of itself, should be counted as success.

IS SECRETARY CUOMO'S 2020 MANAGEMENT REFORM A SUCCESS STORY?

When Secretary Cuomo announced his HUD 2020 Management Reform Plan in June 1997, he said: "For HUD to fulfill its mission, it must have credibility—with Congress, with local government[, with the] customer. They must all believe that HUD has the competence and capacity to perform its functions. It's time HUD put its own house in order." HUD 2020 was Secretary Cuomo's plan to put HUD's house in order.

Since the fall of 1998, Secretary Cuomo has cited increased HUD budgets and positive statements by consultants paid by HUD as evidence that HUD's credibility has been restored. Secretary Cuomo in turn presents this as evidence that the HUD 2020 Management Reform has worked.

Again, the OIG's approach is different. We have tracked the progress of HUD 2020 in as objective a manner as possible, against the goals and time frames Secretary Cuomo established for it. And from this perspective, at this writing, HUD 2020 cannot be called a success. More than 2½ years after its announcement, HUD 2020 is still very much a work in progress.

HUD 2020 was supposed to be fully operational by October 1998. By that time, staffing reductions and organizational changes had been made, but the business process improvements called for by HUD 2020 had not taken place. At this writing, 16 months after the October 1998 deadline, we are still waiting to see the business process improvements. For example:

SINGLE FAMILY PROPERTY DISPOSITION

Earlier in this statement, I talked about the management and marketing contracts, the HUD 2020 device intended to increase the efficiency of HUD's Single Family property disposition function and compensate for severe reductions in Single Family staff. Again, between April 1999, when the management and marketing contractors started work, and January 31, 2000, HUD's REO inventory has increased from 43,560 to 47,711 properties; the percentage of properties in the inventory 6 months or more has increased from 30 to 41; and the percentage of properties in the inventory more than 12 months has increased from 10 to 17.

While there is evidence of a decline in HUD's inventory from a high of 51,537 properties at September 30, 1999, the size of the older inventory has grown from month to month.

SCORING THE FINANCIAL AND PHYSICAL HEALTH OF HUD'S PUBLIC AND MULTIFAMILY PORTFOLIOS

Another key initiative under HUD 2020 is the centralized REAC, whose primary purpose is to score the physical and financial health of HUD's public housing and multifamily portfolios, thus enabling other HUD entities to better target their monitoring and enforcement efforts. The Department budgeted about \$63 million in Fiscal Years 1998 and 1999 and another \$100 million over Fiscal Years 2000 and 2001 to develop all assessment, including the physical and financial assessment systems.

While we consider this comprehensive approach to assessing the HUD portfolio a positive step, we have yet to see evidence that results are being or will be widely used:

- During Fiscal Year 1999, the REAC reported that 28,835 physical inspections of multifamily and public housing properties had been conducted. The Office of Housing has established a procedure to address physical inspection results. However, the procedure relies on owners' certifications to assure that repairs are complete, even in the case of health and safety violations. In contrast, the Office of Public and Indian Housing has generally been reluctant to use the inspection results in their monitoring of the Public Housing Authorities because the scores were only advisory in Fiscal Year 1999. While it is true that the scores to date have been advisory, the physical deficiencies are real conditions—including health and safety violations—that need to be corrected.

HUD has announced that it will start official physical inspections in June 2000. There is, however, significant question about how this intention complies with the following instruction in the Conference Report on HUD's Fiscal Year 2000 appropriations:

"The conferees direct HUD to delay implementing the Public Housing Assessment System (PHAS) until, in consultation with public housing authorities (PHAs) and their designated representatives, the Secretary: (a) conducts a through analysis of all advisory PHAS assessments; (b) reviews the GAO's study of the PHAS when it is complete; and (c) based on that analysis and review, publishes in the Federal Register a new consensus-based PHAS final rule that incorporates any recommended changes resulting from the process referenced above."

To the OIG's knowledge, the GAO study of the PHAS will not be complete by June 2000. At least one major housing interest group is, in addition, claiming that HUD did not comply with the other provisions of the Conference Report language before issuing the final PHAS rule.

- During Fiscal Year 1999, the REAC (REAC) assessed the financial reports for approximately 2,800 Public Housing Authorities and received financial statements for approximately 7,800 insured multifamily projects. The assessment of Public Housing Authorities financial reports is on schedule; however, the assessment was only advisory for Fiscal Year 1999. Consequently, the results of the assessments were not generally utilized by Field Offices.

In contrast, delays were encountered in obtaining electronic submission of insured multifamily projects financial information. The REAC therefore extended the financial statement filing deadline to August 1999 from March 1999, and the Office of Housing delayed releasing the data to the Field Offices until staff could be trained on the use of the data. Distribution of financial results began on September 30, 1999. REAC has advised that all financial information and analyses are now available to the Office of Housing for project monitoring. The OIG has yet to determine how or whether the results are being used.

TAKING ACTION TO IMPROVE TROUBLED PUBLIC HOUSING

Another key initiative under HUD 2020 are two Troubled Agency Recovery Centers, whose mission is to work with public housing authorities designated as troubled by the REAC, in order to assist the housing authorities in bringing their performance to an acceptable level. HUD declared the Troubled Agency Recovery Centers fully operational on October 1, 1998.

In September 1999, about a year later, the OIG looked at the two Troubled Agency Recovery Centers and found they were working at 10 percent of their planned capacity. The reason is simple: HUD had expected that the REAC's scoring systems would identify 575 troubled public housing authorities that would constitute the Troubled Agency Recovery Centers' workload by October 1998. However, at this writing, almost 16 months later, the REAC still isn't issuing official scores, so the Troubled Agency Recovery Center workload is still defined by the former and very deficient self-assessment system known as the Public Housing Management Assessment Program (PHMAP). Under PHMAP, there are only 52 troubled public housing authorities.

Consider what this means. On the one hand, if HUD was correct that its Troubled Agency Recovery Center staff could handle 575 troubled authorities, but their actual workload is only 52, then 90 percent of that staff has been underutilized or not utilized for a long time.

More importantly, HUD doesn't need elaborate Real Estate Assessment scoring systems to know that there are some very troubled public housing authorities that aren't identified as such by PHMAP. Consider the case of the Puerto Rico Housing Administration (PHA).

- In December 1996, HUD took the PHA off its PHMAP-based list of overall troubled public housing authorities. The PHA has never gone back on that list.
- In June 1998, the OIG issued an audit report on the PHA, alerting HUD to a series of potentially serious problems.
- In September 1998, OIG officials told Public and Indian Housing (PIH) officials that there were virtually no controls over the PHA's procurement system, resulting in high potential for fraudulent activity. We urged PIH to intervene immediately to correct PHA business practices. To date, there has been no HUD intervention at the PHA, and the PHA continues doing business as usual.
- On October 29, 1998, based on an investigation by the FBI, OIG, and the Office of the Comptroller of Puerto Rico, three individuals were indicted on charges of conspiracy to defraud HUD and embezzlement of over \$1 million from the PHA. The three individuals have since pled guilty.
- On March 25, 1999, based on an FBI and OIG investigation, six individuals were indicted on charges of bribery, conspiracy, money laundering, and theft of over \$1.4 million in PHA funds. Two of the six individuals have since pled guilty.
- Currently, the FBI and the OIG are investigating five other major cases of potential procurement fraud at the PHA.

TAKING ENFORCEMENT ACTION AGAINST BAD LANDLORDS

Another key initiative under HUD 2020 is the centralized Enforcement Center. At the heart of Secretary Cuomo's "Get Tough" policy, the mission of the Center was to pursue civil and regulatory actions against (i) public housing authorities and private, multifamily owners whose properties receive failing scores from the REAC; and (ii) Community Planning and Development and Fair Housing and Equal Opportunity grantees who do not pass audit scrutiny or who engage in waste, fraud, or abuse.

I expect that the delay in the REAC's issuing official scores for public housing and multifamily properties has negatively affected the Enforcement Center's operations. I am unable to provide you with a definitive assessment, however, because the OIG is just now completing its audit of the Enforcement Center.

I can provide you with two anecdotes that indicate there may be cause for concern.

- In January 2000, as a result of OIG, FBI, and IRS investigative work under the OIG's Housing Fraud Initiative, the U.S. Attorney for the Central District of California announced 41 indictments and guilty pleas for Single Family Mortgage Insurance fraud. Secretary Cuomo promptly issued a press release claiming that the indictments and guilty pleas resulted from his "Get Tough" policy and his establishment of the Enforcement Center. Neither had any relevance whatever to the investigations or the results of the investigations.

- In the spring of 1998, Enforcement Center personnel invited the OIG to assist them in pursuing a \$15 million civil fraud case against Associated Estates Realty Corporation, in Cleveland, Ohio. The case related to Associated Estates' ownership of three HUD-insured, Section 8 subsidized multifamily properties that were notorious, two of the properties having been cited by the City of Cleveland for more than 8,600 health and safety violations.

The OIG agreed with the Enforcement Center's assessment, and an OIG agent accompanied the Enforcement Center personnel to a meeting with the U.S. Attorney's Office. The U.S. Attorney's Office tentatively agreed with the Enforcement Center's assessment, and requested additional information.

The next time the U.S. Attorney's Office or the OIG heard about Associated Estates was from a March 1999 article in the Cleveland Plain Dealer. The article said that HUD program officials (who had taken jurisdiction of the case away from the Enforcement Center) had settled with Associated Estates, agreeing to pay Associated Estates \$1.78 million for the retroactive rent increase on the condition that Associated Estates found new owners for two properties. The Plain Dealer quoted Secretary Cuomo as saying: "This settlement agreement sends a strong message to owners and managers of housing subsidized by HUD. If you don't provide safe and

decent housing to families in need, your days of getting money from this department are over.”

In December 1999, the Plain Dealer reported that HUD had paid the \$1.78 million to Associated Estates, even though Associated Estates hadn't found new owners for the two properties. Howard Glaser, Counselor to the Secretary, was quoted as saying, “Everybody agreed. Let's stop this now, take the properties, even if we have to hold [our] nose and make the payment. The guy who signed it [Gary Eisenman, HUD's General Deputy Assistant Secretary for Housing], would be the first to tell you he held his nose.”

What the Plain Dealer did not report is that, in addition to providing for the \$1.78 million payment for a retroactive rent increase for one property, the settlement agreement also released Associated Estates from any civil or administrative claims relating to their ownership and operation of four HUD-insured and subsidized properties. Three of the four properties were the same properties that were involved in the \$15 million civil fraud case that the Enforcement Center had wanted to pursue.

IMPROVING HUD'S FINANCIAL INFORMATION SYSTEM

Another key initiative under HUD 2020 is the Financial Systems Integration Plan. The Plan was designed to correct Department-wide financial management deficiencies while simultaneously providing the information necessary to carry out the financial and programmatic missions of the Department.

In late 1997, the Department decided to use an off-the-shelf software in the development of its financial management system known as HUDCAPS. In a January 1998 memorandum to the Secretary, we pointed out several risks inherent in that decision. We noted the decision to use the standard software was made without a thorough analysis of other alternatives. Also, the selected software was not user friendly and was not the “state of the art technology” for the time. This year our concerns became reality. After much effort, schedule delays, frequent scope changes, and cost increases, HUDCAPS was prepared to operate as Department-wide ledger beginning with fiscal year 1999. However, as implemented, the HUDCAPS core financial system still does not fully comply with Federal financial system requirements and still does not correct long standing financial system weaknesses in its feeder systems such as the FHA general ledger.

The following financial management systems deficiencies, which were reported in prior years, were present during fiscal year 1999.

- Insufficient information about individual multifamily loans. The financial system cannot identify high risk and troubled loans for monitoring and oversight.
- Lack of integration between program and accounting systems. For example, monthly cash reconciliations are not being done and FHA summary transaction data are not entered into the department-wide system on a timely basis.
- Inability to support adequate funds control for FHA, which, among other things, resulted in an Anti-Deficiency Act violation in fiscal year 1999.
- Inability to fully support budgeting for Section 8 project-based programs. HUD was to do an initial recapture of unneeded excess funds remaining on expired contracts in August, 1999 but was not able to complete that recapture until December due to the systems problems. Moreover, that recapture excluded 391 expired contracts with \$408 million in reserve budget authority because of insufficient data to perform the analysis.

SHOULD THE ANNOUNCEMENT OF NEW PROGRAMS BE CONSIDERED A SUCCESS STORY?

The OIG has long held that there is a mismatch between the number and complexity of HUD's programs and the capability of HUD staff to administer those programs. In 1994, at the request of Secretary Cisneros, we prepared a major report on “Opportunities for Terminating, Consolidating, and Restructuring HUD Programs.” The report was a principal basis for Secretary Cisneros' Reinvention Blueprint, which called for a radical restructuring of HUD programs. You may remember that prospects for enactment of the Reinvention Blueprint ended when the cries for abolishment of HUD began.

When we did our 1994 report, we counted 240 separable HUD program activities. Our last count, in 1997, was 328 separable HUD program activities. We believe the count has continued to increase while HUD staff has continued to decrease.

Against this background, you can understand why the OIG does not consider it good news when Secretary Cuomo announces the “teacher next door” initiative, the “officer next door” initiative, the gun buyback initiative, the Pine Ridge initiative, the HUD storefront initiative, the gun safety initiative, the “healthy homes” initiative, or the initiative to organize public housing authorities to file suit against gun

manufacturers. On its own, each of these initiatives may have some appeal, but their effect is to divert scarce HUD resources away from HUD's core programs.

The diversion of HUD resources away from HUD's core programs has been particularly apparent in the case of the Community Builder Program, a key initiative under HUD 2020. Our September 30, 1999 audit of the Community Builder Program evaluated Community Builder hiring practices, reviewed their assigned duties and responsibilities, and examined their impact on other HUD organizational elements. Our audit found serious problems with Community Builder hiring practices, the Community Builder concept, and the Community Builder's impact on HUD operations:

- There was little evidence to support HUD's decision that it needed about 800 Community Builders. This issue is of importance because the Community Builder positions were established within the framework of HUD's downsizing staff. That is, HUD neither sought nor obtained increased funding for the Community Builders.
- HUD violated Office of Personnel Management rules in hiring "external" Community Builders (who were not HUD staff at the time) as term appointments.
- While the Community Builder concept was part of an attempt to distinguish HUD outreach and monitoring functions, it proved to be an expensive and controversial solution. A common problem identified in many of our recent audits of HUD programs is the lack of staff resources to effectively manage and monitor. The nearly 800 Community Builder staff committed to outreach functions, are a major drain on potential monitoring resources.
- In reviewing the impact of Community Builder work, we found few measurable results. In our interviews with 59 Community Builder staff, 39 said they spent more than half their time on public relations activities.

Our audit recommended the Community Builder program be terminated.

SHOULD POSITIVE ASSESSMENTS BY CONSULTANTS PAID BY HUD BE CONSIDERED
AUTHORITATIVE?

Because HUD 2020 has had a staggering impact on the Department, the OIG has been monitoring its progress on a realtime basis. While OIG work must by law be conducted in accordance with professional standards that ensure its independence and objectivity, the consultants paid by HUD are not governed by such strictures. Once commencement of OIG HUD 2020 work is announced, it has become almost standard operating procedure for the Department to hire a consultant to provide a contemporaneous assessment. Here are a few examples:

Our assessment of the HUD 2020 Management Reform Plan, as described in Chapter One of our September 1997 and March 1998 Semiannual Reports to Congress, was contrasted with a \$412,000 assessment by Booz-Allen & Hamilton and their sub-contractors to include David Osborne and James Champey. Our analysis was an effort to review the progress of organizational changes against HUD 2020 plans and we were critical of major delays in reform implementation. On the other hand, the contractor's assessments were conceptual, focusing on the soundness of the reform concepts. Since Booz-Allen & Hamilton's report was issued in March 1998, it has been used on numerous occasions by HUD management to acclaim the success of HUD 2020 Reforms.

In Chapter One of the OIG's September 30, 1998 Report to the Congress (which was sent to the Congress on December 11, 1998), we tracked the progress of HUD 2020 against milestones that HUD had announced at the outset of HUD 2020. We reported that most of the reform initiatives were well behind schedule. For example, the HUD 2020 Plan had called for the Troubled Agency Recovery Centers to be fully operational by October 1, 1998; but OIG auditors found that the Troubled Agency Recovery Centers were operating at only 10 percent of capacity. On October 30, 1998, the Department contracted with Price Waterhouse Coopers for a \$126,000 evaluation of HUD's progress in meeting seven HUD 2020 milestones. However, in the process, HUD refined the milestones substantially, enabling a positive assessment of progress by Price Waterhouse Coopers on December 1, 1998. In the case of the Troubled Agency Recovery Centers, for instance, the refined milestone was that two Troubled Agency Recovery Offices would be opened by October 1, 1998. In the OIG's view, there is a vast difference between opening offices and ensuring that those offices are fully operational.

Our recent comprehensive review of the Community Builder Program was contrasted with a simultaneous \$146,000 Analysis of Community Builder Effectiveness by Ernst & Young. Under their engagement parameters with HUD, Ernst & Young was provided a list of Community Builder case studies to sample and a list of interview sources. The scope of their engagement did not provide for interviews of HUD employees regarding the Community Builder Program. Our review included inter-

views with 231 parties involved in the program to include Community Builders, other HUD staff and outside customers. The findings in both reports were strikingly different.

ARE INCREASED APPROPRIATIONS FOR HUD A SUCCESS STORY?

Since being confirmed as Secretary of HUD, Andrew Cuomo has said that HUD must get its own house in order before it could expect to be entrusted with new programs and/or increased budgets. As I said at the start of this testimony, Secretary Cuomo along with other Principal Staff, notably Deputy Secretary Ramirez, have declared much of the 2020 Management Reforms a success. They have taken advantage of opportunities the Congress has provided them to testify as well as announcing the results of studies they have contracted for as vehicles to communicate this.

Just 10 days ago the HUD Public Affairs Office issued a press release announcing the President's 2001 Budget. The press release contained the following statements by Secretary Cuomo:

"This budget shows that HUD is back in business, and has achieved a new level of public trust and confidence by proving it can create and run quality programs;"

"The budget will build on HUD's success and help unlock the door to prosperity for people and places left behind in these good economic times;"

"Just a few years ago, our critics were calling for the elimination of HUD;" and, "Today, HUD is held up as a model of successful government reinvention."

The Secretary should be congratulated for both his acumen and persistence in conveying the budgetary needs of HUD's constituents and his success in attaining increased appropriations. For Fiscal Years 1999 and 2000 the Department's efforts were recognized with increased appropriations: the best HUD budgets in 10 years was the Secretary's message. The President's 2001 Budget continues this trend with a proposed increase of \$6 billion. As I said earlier, we in the OIG believe in HUD's mission. HUD is the hope of last resort for many folks living in this Country, and few people convey that message as convincingly as Secretary Cuomo.

Conversely, staff in the OIG routinely see first hand the waste and abuse of scarce HUD funds. HUD could do a much better job with the resources it has if it dealt more with the substance, that is the infrastructure, rather than the ministerial aspects of reform. In other words, HUD needs to deal with the material weaknesses and not just the checkbook balance if it is to assure that increased funding truly assists the rightful beneficiaries.

YET AGAIN, SO WHAT?

I support many of the goals that Secretary Cuomo has for HUD. I trust it is clear to you, however, that Secretary Cuomo and I have very different views about the current state of affairs at HUD. To some extent, that is not surprising: Secretary Cuomo, understandably, wants to tell a success story; but my job is to report the facts, including problems, and encourage problem-solving when appropriate. As I said at the outset of this testimony, an IG's view is a particular view, but I believe it is critically important that HUD identify and solve its problems in order to better serve the people who need HUD's help.

The media have tended to label Secretary Cuomo's and my differing views as a personal feud. That perception is highly unfortunate, but I think it arises because Secretary Cuomo and I seem to be the only people, other than GAO, engaging in any dialogue about waste, fraud, and abuse at HUD. And that doesn't make any sense to me.

First, I think it goes without saying that no cabinet department should be an island unto itself. Yet ongoing Congressional and Executive Branch oversight of management issues at HUD is minimal, at best. Your hearing today is, to me, a relatively exceptional expression of interest by the Congress. For its part, the Office of Management and Budget (OMB) tends to track a small number of narrow issues. OMB, for instance, exerts considerable pressure on agencies to obtain unqualified opinions on audits of financial statements, but I am aware of no equivalent OMB interest in the accompanying Report on Internal Controls. Yet we know that Congressional and Executive Branch oversight can be very effective: witness the Y2K success story.

Second, I don't think HUD can solve its problems all by itself. I am not opposed to downsizing the Federal bureaucracy, but we should be determined that the downsized bureaucracy has the capacity to administer its programs. And that, to me, means that we should be looking for every opportunity to consolidate, terminate, and streamline programs. We should be considering increased use of formula and block grants. We should be talking again about devolution of responsibilities to States and localities, a concept that hasn't made much progress at HUD. We should

be looking for ways to build incentives into programs that work to prevent fraud, waste, and abuse, thus requiring less onerous and unappreciated monitoring by the Federal Government. We should be thinking about whether Government Corporations such as Ginnie Mae and FHA should be allowed to truly operate as government corporations and, in the process, solve their own management problems.

Obviously, such actions would require intensive, ongoing efforts on the part of the Congress and the Executive Branch. But, in my view, the benefits would far outweigh the costs.

Mr. Chairman, that concludes my testimony. I appreciate the opportunity you have afforded me to appear here today.

ADDENDUM SUBMITTED BY SUSAN GAFFNEY, INSPECTOR GENERAL, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

OFFICE OF INSPECTOR GENERAL,
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT,
Washington, DC, February 23, 2000.

Hon. JOHN KASICH,
Chairman, House Budget Committee, House of Representatives, Washington, DC.

DEAR CHAIRMAN KASICH: Thank you for the opportunity to present my views on governmental fraud and waste to the Committee and for the courtesy extended to me and my Inspector General colleagues by the Chairman.

In part, my testimony was based upon ongoing audits and investigations. Because of this, I am revising my written testimony concerning an FHA violation of the Anti-Deficiency Act (see Page No. 10 of the Statement). As I was testifying, the OIG's contract independent auditors were discussing the violation with Office of Management and Budget (OMB) officials. Based upon those discussions and a unique automatic apportionment provision for the payment of credit financing interest to the U.S. Treasury in OMB Circular No. A-34, the independent auditors have concluded that the provisions of 31 U.S.C. 1517 do not apply to the type of payment that FHA made. We agree with this conclusion.

The part of the same statement pertaining to FHA's inadequate funds control is still accurate. The independent auditors still consider this a material weakness. The same transaction was improperly recorded and reported by HUD necessitating a change to their September 30, 1999 financial statements. Moreover, at the direction of OMB, both the HUD Deputy Chief Financial Officer (CFO) and FHA's Comptroller are devising, with the help of consultants, a plan to establish funds control at FHA. According to the Deputy CFO, two new FY 2000 appropriations have been placed under an improved funds control system and agreement has been reached with the FHA Comptroller on the handling of FHA field budget accounts that is to be implemented this fiscal year.

Should you or your staff have any questions or concerns over this matter, please feel free to contact me.

Sincerely,

SUSAN GAFFNEY,
Inspector General.

Chairman KASICH. Thank you very much.

STATEMENT OF DONALD MANCUSO

Mr. MANCUSO. Mr. Chairman, I guess after the previous two speakers, I will do my remarks in a much briefer form as well. I think much of what I was going to say was actually discussed earlier—

Chairman KASICH. Let me just tell you, sir, at home now I barely get to speak. [Laughter.]

So go ahead.

Mr. MANCUSO. Well, again, this committee is well aware of the size of the Department of Defense and the many problems that are faced there. In that light, by the way, I would also like to take a minute just to thank the committee for the Wastebusters website. We have received about three dozen tips so far, and, based on some of them, we recently initiated what will be a major review involving the Standard Procurement System, which is a new system that

is intended really to bring our ability to track procurements into this century.

Chairman KASICH. Have these, if I could interrupt you, proved to be useful to you?

Mr. MANCUSO. Most certainly.

Chairman KASICH. They are.

Mr. MANCUSO. Most certainly, Mr. Chairman. And I know we will be responding, as the other IGs will, as well. Some matters, I suspect, will warrant full-scale reviews, while others clearly may not. But certainly the added information is useful to us.

In your request involving this hearing, you asked that we also comment on management's response to IG findings. Before I speak to the larger issues facing the Department, I just wanted to put into some perspective how the Department is responding overall to reviews and audits of the Department, and more particularly to the DOD IG audits and evaluations.

The news is generally good. Management has been very responsive. When it comes to the DOD audit recommendations, and we have had about 1,000 of them emanating from about 250 reports a year, or about 2,000 recommendations in the last 2 years. About 97 percent have been favorably received and accepted by management. Now, does that mean that management quickly implements those recommendations that they have agreed to? No, I am sorry to say the answer to that is not always. They usually do. There are some significant exceptions where they have not, but we have a follow-up procedure where we work with management to address those things and, in fact, the letters from Congress each year on this topic are welcome to us. We can actually go back and report where management has not yet complied with some of the recommendations. However, I would like to state that my main concern is not with management inaction on audit advice, but rather the inadequate audit and investigative coverage of many high-risk areas due to our resource constraints.

I would like to start with some of the ten items that we identified in responding to your committee's request that we comment on major problems facing the Department. One of the topics, and again it was discussed earlier today, is information technology. Information technology in the Department of Defense is big business. We are talking about \$16 billion a year in acquisition, maintenance and the running of these systems.

Less than ten of the Department's major IT acquisition programs have been audited in each of the past couple years. That is unbelievable when you consider the hundreds of different programs that are out there. Additionally, the Department has been a bit slow in complying with the Clinger-Cohen Act. It is good news that there has been some recent progress in that direction, but we still see major vulnerabilities in the Department because of its past lack of attention in coordinating and pushing forward in the concept of Clinger-Cohen.

We have also found in the area of information technology that, as large as we are with as many systems as we have in the Department, we are clearly vulnerable to attack by hostile regimes and others. The Defense Information Security Agency reported that there were about 18,000 cyber attacks on DOD computers last year.

DOD is the leader in cryptology in the world. So the classified systems are well protected, but there is a significant problem with security of unclassified systems. We are working that area. We have our own team of computer intrusion people, and we work with other agencies as well in that regard.

One of the most significant areas facing the Department, though, is financial statement review. It has been pointed out that the Department of Defense has been extraordinarily behind the curve in being able to achieve unqualified audit opinions on financial statements. As Mr. Walker pointed out, the Department is really not prepared to achieve an unqualified opinion on its overall statement until at least 2003. We only have one of the 10 major statements currently receiving unqualified audit opinions, and that is the Military Retirement Trust Fund.

What is behind this, however, is a lack of adequate accounting systems; and modernizing them, and getting them to talk to each other so that we can have clean opinions. There were \$1.7 trillion in unsupported adjustments last year involving Department of Defense financial statements.

Chairman KASICH. Could I just interrupt to ask you a question? Why is this the case? Is there some explanation for this?

Mr. MANCUSO. The explanation is that, for an extended number of years, finance and accounting procedures were extraordinarily decentralized. Hundreds of systems have operated independently. Over the last decade, there has been massive consolidation related to the formation, for instance, of the Defense Finance and Accounting Service, and a great reduction in numbers of systems has taken place. Unfortunately, much more needs to be done.

The size of the systems and the amount of dollars involved is causing it to take a number of years to develop, test and field the systems that are going to be necessary for the Department to have data that can be relied upon. One of the outgrowths of this is this huge amount of unsupported adjustments. That would be wholly unacceptable in a business.

If you were running a business, your accounting firm would be aghast to find even more than just a few adjustments, much less unsupported adjustments. But in the case of DOD, as someone stated earlier, there is a plugging in of the figures. We found that last year there were actually about \$7 trillion of adjustments. Of the ones we audited, which were about half, we found that about \$1.7 trillion were unsupported; in other words, there was not enough basis in the accounting records to support those adjustments.

Chairman KASICH. One more follow-up. What does that mean? What does that mean to the practical side of what we are doing on a day-to-day basis?

Mr. MANCUSO. If you are a war fighter, if you are a person who is performing the DOD mission, it probably doesn't mean very much because things are still going on, missions are being accomplished, and DOD operational managers have little need to refer back to the financial statements.

In truth, however, the same information that is lacking to produce a good financial statement is the information that managers generally need to efficiently and effectively run programs. So

there is, of course, a real and serious impact overall on DOD management and the efficiency of it.

We have been pointing out for several years now that the Department, although it is moving forward, needs a more consolidated and consistent approach. We have worked on a regular basis with the Department on this challenge. For example, there was a meeting earlier this week with GAO, OMB, our office and the comptroller's office, again, trying to keep these processes online. But we see little hope for clean opinions for the statements in some of these major accounts until 2003.

There have been some comments today on the military health care system. In DOD, that is a \$16-billion-a-year business, serving about 8 million beneficiaries. They have made great progress in the area of managed care. They have worked closely with us in building in internal controls; nonetheless, there is a huge amount of fraud. We work very closely with HHS and the Bureau on those things. But, yes, the amount of fraud in that area is still rather significant.

Logistics is another area of concern. There are about 300 ongoing initiatives to make it more efficient. Still, much more needs to be done. You can look at it as a success story or a failure, but in the last 10 years, the wholesale stock supply has been reduced by about half, to \$55 billion. Nonetheless, of that \$55 billion, there is much that isn't needed or is antiquated or otherwise being held in an inefficient way. There are also initiatives that will bring us forward in transportation and other logistics areas.

I could speak at great length about readiness concerns, but I think they are topics you are all familiar with. The main thing I would point to in the area of readiness, and I don't believe Mr. Walker pointed to it, is really the operational tempo.

The operational tempo has made it extraordinarily difficult for the people in logistics to gauge what parts, supplies, and equipment we need. You have the Air Force, for instance, putting 2 years' worth of flight time on aircraft during a 6-month deployment to Southwest Asia. That presents problems that are not easily forecast. You have training problems and readiness shortfalls in other areas as well. Again, those items are detailed in my statement, Mr. Chairman.

I think I will just end right there, please.

[The prepared statement of Donald Mancuso follows:]

PREPARED STATEMENT OF HON. DONALD MANCUSO, DEPUTY INSPECTOR GENERAL,
U.S. DEPARTMENT OF DEFENSE

Mr. Chairman and members of the committee, I appreciate the opportunity to be here today to discuss the management challenges faced by the Department of Defense (DOD) and the responsiveness of its managers and commanders to findings and advice provided by the Office of the Inspector General, DOD.

The Committee needs no reminder that the DOD is one of the largest and most complex organizations in the world. The Department is responsible for roughly \$1.3 trillion in assets; operates 638 major installations and thousands of small sites around the world; and currently has about 700,000 civilian employees and 2.4 military personnel in the active forces or the Ready and Standby Reserves. Thousands of programs and projects are needed for the Department to successfully execute operations across the spectrum from warfighting to peacekeeping as well as humanitarian and emergency relief operations. Critical functions include: research and development; procurement; logistics; intelligence; and a wide variety of other activities to train, equip and sustain the Armed Forces.

There has been widespread concern about waste and inefficiency in military programs throughout this nation's history. Although it is doubtful that efforts to equip and support the Armed Forces are inherently more susceptible to fraud or mismanagement than other government activities, the size and complexity of the Department of Defense pose formidable management challenges and risks. The Department's own assessments of the need for reforms, oversight by the Congress, General Accounting Office reports, and the work of the DOD audit and investigative communities show that a wide range of problems currently merit attention and action. We welcome additional measures, such as the Committee's Wastebusters website, to help identify problems and risks. Tips that you refer to us from the Wastebusters website will supplement those received on our own DOD Hotline, which averages 14,000 calls annually.

A few weeks ago, you referred about three dozen e-mail tips received at the Wastebusters website to my office for review. We appreciate every new source of leads for possible audits and investigations. I assure you that we are taking the Wastebusters tips seriously and will keep the Committee fully informed on the disposition of each one. For example, because three Wastebusters tips concerned the new DOD Standard Procurement System (SPS), we have initiated an audit of SPS implementation at Air Force sites.

Another welcome recent congressional initiative was the joint letter in September 1999 from the House Majority Leader, the Chairmen of the House Government Reform Committee, Senate Budget Committee and Senate Governmental Affairs Committee, and you, Mr. Chairman, on DOD management challenges. Specifically, you requested we update our previous assessments of the most serious management problems facing the DOD; identify related reports; summarize significant audit recommendations that address major problem areas; comment on progress made in implementing audit recommendations and correcting management problems; and identify programs that have had questionable success in achieving results. Although we have worked to include much information of that kind in our semiannual reports, we appreciated the additional opportunity to discuss the results of our oversight efforts.

Our December 15, 1999 reply to the joint inquiry discussed groups of often inter-related problems which we sorted into ten principal management challenges, as follows:

1. Information Technology Management
2. Information Technology Security
3. Other Security Concerns
4. Financial Management
5. Acquisition
6. Health Care
7. Supply Inventory Management
8. Other Infrastructure Issues
9. Readiness
10. Turbulence from Change

DOD MANAGEMENT RESPONSIVENESS

Before discussing each area, I would like to address the overall question of DOD responsiveness to the need for reform and the specific issue of how well managers respond to Inspector General, DOD, advice.

Starting in the late 1980's and continuing through the 1990's into the present day, the DOD has been attempting to restructure virtually all of its internal processes. The Congress has been closely involved in dozens of specific initiatives, particularly in the area of acquisition reform. Our overall assessment is that the DOD has seldom, if ever, been so committed to across the board management improvement. However, even after several years of concerted effort, progress has been mixed and much more needs to be done to cut costs and improve effectiveness.

To identify specific problems and monitor improvement efforts, the Department performs a huge number of self-assessments, including thousands of internal audits and inspections annually. Those assessments include about 250 audit and evaluation reports with about 1,000 recommendations each year from the Office of the Inspector General, DOD.

To respond to the problems identified by audits, management reform studies and other reviews, the DOD is carrying out many hundred major management improvement initiatives simultaneously. Cumulatively, and with continuous management emphasis, those initiatives should dramatically improve the efficiency of DOD support operations over the next several years. We also believe that, on an overall basis, the Department is being very responsive to audit advice as it develops and

carries out these management improvements. For example, managers agreed to take responsive action on 97 percent of the 2,040 audit recommendations made by this office during fiscal years 1998 and 1999. We do not have comparable information from earlier periods, but senior auditors in my office believe that this compliance rate is far higher than was the case during the earlier years of the OIG, DOD. We do not expect to win every battle and it would be unreasonable to expect agreement with every audit recommendation, nor is it realistic to expect timely implementation of every agreed-upon recommendation. The majority of agreed-upon actions are carried out within reasonable timeframes, but significant exceptions do occur. Nevertheless, we believe that the very high level of acceptance of our recommendations and reasonably good follow-up record speak well for both the auditors' performance and the receptiveness of managers to the audit advice they receive.

The main concern with the effectiveness of auditing in DOD relates not to management inaction on audit advice, but to the inadequate audit coverage of many high risk areas because of resource constraints and conflicting priorities. I will elaborate on that concern later when I discuss the top management challenges.

INFORMATION TECHNOLOGY MANAGEMENT

Information technology is transforming both military science and business practices. The DOD operates about 10,000 mission critical or essential networks and is rapidly expanding its use of web-based technology for electronic commerce and other "paperless" functions. The annual budget for information system development, procurement, operation and maintenance is about \$16 billion, but even that large figure does not fully portray the paramount importance of information systems to virtually every facet of managing the Armed Forces and their support establishment.

The DOD badly needs to complete its implementation of the Clinger/Cohen Act. Appropriately, there has been increased congressional interest recently in turning around the long-standing problem of inadequate management control over information technology investments, standards and practices. The Defense Appropriations Act for Fiscal Year 2000 levied stringent new requirements on the Department to ensure a complete break with overly decentralized and often inefficient practices for reviewing, approving, monitoring and funding automated system acquisition projects. Better management is needed to avoid costly acquisition failures of the 1990's like the Army Ground Based Common Sensor System and Defense Commissary Information System.

Currently, less than 10 of the Department's hundreds of "IT" acquisition projects are being audited annually. Now that the massive Y2K audit effort is behind us, it is vitally important to provide more oversight in this area.

We are currently working with senior DOD managers to develop a more active audit effort, resources permitting, to support and fine tune the Department's management control processes for IT system acquisition. Successful implementation of effective management oversight processes will help avoid recurrence of most information system problems currently evident in the DOD. Those problems include: too many systems; block obsolescence; insufficient interoperability; security vulnerabilities; inconsistent budgeting and reporting; noncompliance with policies on data standardization, documentation and configuration management; user dissatisfaction; frequent system acquisition schedule slippage and cost overruns; and disconnects between evolving business practices and their supporting system projects.

In addition to improving management of system acquisition, the Department needs to modernize and cut support costs for communications and other information technology infrastructure. The Y2K conversion has forced the acceleration of efforts to replace and modernize various equipment, including DOD telecommunications switches throughout the world, and the increased awareness of the Department's dependence on information technology should focus more attention on related infrastructure issues.

Overcrowding of the radio frequency spectrum throughout the world presents a particularly difficult challenge to military planners and users of weapon and communication systems. We reported in October 1998 that at least 89 weapons and telecommunications systems had been deployed overseas without the proper frequency certification and host nation approval. In addition, the Military Exchange stores were selling products not covered by, or compliant with, host nation frequency agreements. As a result, communications equipment deployed without host nation approval and frequency assignments cannot be used to its full capability for training, exercises or operations or without risking damage to host nation relations. Potential frequency spectrum conflicts should be considered during system design, when host nation agreements are negotiated and before systems are deployed. The

DOD also needs a more systematic process to update telecommunications agreements with other countries, clarification of accountability for managing those agreements and more emphasis on compliance with them. The most recent register of telecommunications agreements was over 4 years old, at the time of the audit.

INFORMATION TECHNOLOGY SECURITY

The heavy dependence of the public and private sectors on computer technology for processing sensitive information, controlling infrastructure ranging from air traffic control systems to power grids, and supporting modern communications makes information warfare an attractive strategy for hostile regimes and groups. Hackers view accessing or vandalizing Government information systems virtually as a sport, and there is a significant threat that criminals will exploit information system security weaknesses to steal data or funds. The Defense Information Systems Agency states that over 18,000 cyber attacks against DOD were detected in FY 1999, a three fold increase over the previous year. While this increase is partially attributable to more effective detection, there is probably more activity in this arena.

The DOD internal audit community, GAO and other reviewers have outlined DOD information assurance challenges in numerous reports. To meet those challenges, the Department needs to adapt lessons learned from the Year 2000 conversion effort; consolidate and update policy guidance; establish better management control over the many separate efforts now under way or planned; develop reasonable program performance measures; ensure full attention to information assurance concerns in new system development and electronic commerce initiatives; intensify on-site information security inspection and audit efforts; and improve training across the board for technical personnel, security officers and system users. The DOD is turning increased attention to these matters, but a sustained effort will be needed on a continuous basis for the foreseeable future. The DOD audit and investigative communities are working cooperatively with DOD management to provide support in this vital area. These include the establishment of the Defense Information Infrastructure Intrusions Investigative Team (DI4T) by the Defense Criminal Investigative Service to provide immediate criminal investigative response to suspected computer intrusions against the DOD Information Infrastructure (DII). The DI4T is an integral part of the law enforcement-counterintelligence cell of the DOD Joint Task Force-Computer Network Defense (JTF-CND) that provides for the coordination and overall situational awareness of all law enforcement and counterintelligence activities within the DOD conducted in support of the computer network defense and the DII. The DCIS and DOD are also represented and maintain an active role in the operation of the National Infrastructure Protection Center (NIPC) at the Federal Bureau of Investigation.

OTHER SECURITY CONCERNS

In addition to the challenge of protecting access to information systems, the DOD received new indications that its procedures for minimizing security risks from within its own workforce and contractor personnel also needed improvement. In October 1999, the GAO reported severe problems at the Defense Security Service (DSS), which handles DOD personnel security investigations. The GAO faulted the timeliness and quality of DSS investigations and highlighted a backlog of several hundred thousand cases. The DOD agreed with all GAO recommendations and had already replaced the Director, DSS. We are following up on the agreed-upon recommendations and attending periodic DSS management reviews to monitor the status of corrective actions. We also are participating in a DOD study of alternatives for reducing the backlog of clearance investigations and we are completing audit work on several related issues. We plan a series of four reports over the next several weeks.

The United States Government controls the export of certain goods and technologies by requiring export licenses for specific dual-use commodities or munitions. In the wake of the Cox Commission Report and other disclosures, congressional and media attention has focused on the dangers to national security posed by an export licensing process that is often alleged to favor commerce over national security. Meanwhile, Defense industry and friendly countries are critical of the current slow and unpredictable license review procedures.

The Government needs an export licensing and technology transfer program that protects critical military capabilities through timely and reasonable reviews but also supports Defense cooperation with allies and friends. In an effort to strengthen security and export controls and to accelerate the review process, the Deputy Secretary of Defense approved an Arms Transfer/Technology Transfer White Paper on September 30, 1999, which kicked off an effort to reengineer the DOD process for reviewing license applications. However, the DOD cannot unilaterally revamp the

multiagency license review process and attaining interagency consensus in this area is very difficult.

Additional challenges facing DOD in this arena include determining personnel requirements and addressing the marginal adequacy of the Foreign Disclosure and Technical Information System (FORDTIS), the principal automated tool for DOD export control analysts. The DOD also has no overall capability for analyzing the cumulative effect of exports and other technology acquisitions upon other countries' military capabilities, even though this information is critical to evaluating risks inherent in proposed exports. Commenting on an IG, DOD, draft report, the Department generally agreed with our recommendations for process improvements; however, the new DOD review of the entire process may result in some of our recommendations being overtaken by events. Currently, we are concentrating on meeting the multi-agency audit requirements mandated by the Congress in the National Defense Authorization Act for Fiscal Year 2000. This year, our review is focused on controls in DOD laboratories and other facilities over information released to foreign visitors. We will submit our report in March.

FINANCIAL MANAGEMENT

The DOD continues to be unable to prepare financial statements that can withstand the rigors of audit for most individual major funds and the overall Department. For FY 1998, as in previous years, only the Military Retirement Trust Fund received a favorable audit opinion. It is unlikely that the audit results on the financial statements for FY 1999 will be significantly different when we issue our reports in late February. The DOD financial statements for FY 1998 were less timely than ever and a record \$1.7 trillion of unsupported adjustments were identified by auditors. This startling figure reflects the continued lack of integrated, double-entry, transaction-driven, general ledger accounting systems. The laborious workaround procedures still needed to compile the financial statements are simply inadequate.

The inadequacy of current systems continues to be the major impediment to achieving favorable audit opinions and producing reliable financial reporting. Major changes are necessary to ensure that over 200 complex accounting and feeder systems can produce auditable data. For this reason, DOD does not expect a significant improvement in the overall results of financial statement audits for several more years, although individual segments of the Department are beginning to show progress.

The DOD made a credible attempt to meet several congressional reporting requirements with the first Biennial Financial Management Improvement Plan, September 1998. In April 1999, we reported our assessment of the Plan. Its primary weakness was a lack of information on the status of efforts to achieve compliant systems. This lack of specific data indicates insufficient overall DOD management control over the financial systems remediation process. The Department agreed with our recommendation to adopt lessons learned from the Year 2000 conversion regarding a central management plan, standardized reporting for every system and periodic senior management review. However, implementation of that concept has been disappointingly slow. Nor does the Department appear to be making a concerted effort to comply with the congressional requirement for a wall-to-wall property inventory this year, which is needed to enable accurate financial reporting regarding DOD property.

Audits also continue to indicate problems related to cash management and rate setting in the DOD working capital funds, inaccurate or untimely recording of obligations and disbursements in accounting records, and inability to eliminate unmatched disbursements. In addition, internal controls in disbursing offices need improvement to reduce vulnerability to fraud. As of September 30, 1999, the Defense Criminal Investigative Service had 85 open financial fraud cases. We have worked closely with the Defense Finance and Accounting Service to improve their fraud control program, but contractor payment processes remain vulnerable to fraud and error. Last year, contractors voluntarily refunded \$97 million of over payments. No one can tell how many inaccurate or fraudulent payments were made, but not detected.

ACQUISITION

In fiscal year 1999, the DOD purchased about \$135 billion in goods and services, using more than 250,000 contracts, grants, cooperative agreements and other transactions. Because of its huge scale and impact on US military capability, the DOD acquisition program has always been controversial. There have been nearly continuous reform efforts over the past 20 years to reduce costs and acquisition lead time or to address the myriad of other issues present in this area.

Resource constraints, numerous mandates and requests for internal audits in other management areas, and the long-standing comparative reluctance of DOD acquisition officials to request audits have severely curtailed internal audit coverage over the last few years. This is particularly true for the several hundred ongoing weapon system acquisition programs. Although the largest of those programs are frequently audited by the General Accounting Office, very few of the small and medium size programs are receiving audit coverage. Available resources are insufficient to support a systematic program of comprehensive internal auditing based on risk analysis. Similarly, the 39 percent reduction of the Defense Contract Audit Agency between 1990 and 1999 has limited contract audit coverage.

Although recent audit coverage on many acquisition programs, issues and initiatives has been limited, we have been actively involved in numerous DOD acquisition reform process action teams and task forces. We have commented extensively on proposed acquisition legislation and regulatory changes. We have also performed in-depth audits of some acquisition issues of particular interest to the Department and Congress. Those issues include spare parts pricing, defense industry consolidation, and the use of multiple award task order contracts.

The IG, DOD, supported the acquisition reform laws passed during the 1990's. Further refinements to those laws and others governing DOD acquisition practices should be welcomed and fully considered. However, we urge that the primary focus for the near term be on fully implementing and assessing the impact of the recently enacted changes, as opposed to proposing more changes just to maintain a sense of momentum.

Determining the impact of the enacted legislative and regulatory changes and of numerous ongoing acquisition initiatives is often hampered by slow implementation actions, insufficient experience to date using the new practices, uncertainty on whether implementation was complete or properly done, a lack of specified performance metrics and the absence of independent validation of reported results.

Audits continue to indicate problems in the Department's attempts to comply with reform legislation, specifically in the area of adopting commercial buying practices and establishing equitable business relationships with contractors for spare parts. When genuine competition exists, market forces drive prices down. However, when competition is limited or non-existent, there are no equivalent market forces and in sole-source purchasing the Department frequently pays exorbitant prices.

Our audit coverage over the past 2 years has been concentrated in the historically high risk area of aviation spares, but the same problems likely pervade other commodity areas. The DOD has been slow in providing adequate guidance and training to contracting officers. There continues to be too much emphasis on weakening the Truth in Negotiations Act, the primary safeguard of the Government's interest when competition is lacking. On the other hand, the Department is attempting to establish more reasonable, long term arrangements with several key suppliers and useful models may result from those efforts. We will issue additional reports on this matter over the next few months.

Throughout the 1990's, most acquisition reform emphasis was on systems and hardware procurement. The DOD has realized that purchasing services, such as management consulting, information system maintenance, testing support and environmental cleanup, deserves equal emphasis. We believe that, in many ways, contracting for services is intrinsically harder than for systems or equipment, yet training for contracting personnel in this area is deficient. The DOD spent over \$50 billion for services in 1999, so it is important that controls be adequate and decision making be sound.

We are gratified by the quick response of the Congress, Office of Federal Procurement Policy and DOD to our report that multiple award task order contracts were being misused to avoid competition. We will issue a comprehensive report on services contracts in a few weeks. Likewise, we are assessing the impact of downsizing on the DOD acquisition work force and will issue a report in the near future.

HEALTH CARE

The Military Health System (MHS) costs nearly \$16 billion annually and serves approximately 8.2 million eligible beneficiaries through its health care delivery program, TRICARE. TRICARE provides health care through a combination of direct care at Military Department hospitals and clinics and purchased care through managed care support contracts. The MHS has dual missions to support wartime deployments (readiness) and provide health care during peacetime.

The MHS faces three major challenges: cost containment, transitioning to managed care, and data integrity. These challenges are complicated by the inadequate information systems available to support the MHS.

Cost containment within the MHS is challenged by the continued lack of good cost information combined with significant levels of health care fraud. Lack of comprehensive patient-level cost data has complicated decisions regarding whether to purchase health care or to provide the care at the military treatment facility.

To combat health care fraud, the Defense Criminal Investigative Service has developed an active partnership with the TRICARE Management Activity to give high priority to health care fraud cases, which comprise a growing portion of the overall investigative workload. As of September 30, 1999, we had 531 open criminal cases in this area. The following examples of recently closed cases show the kinds of improper activity being encountered.

- Genentech, Incorporated, of San Francisco, California, was sentenced to pay the Government a total of \$50 million to resolve issues related to the introduction of misbranded drugs in interstate commerce. Genentech admitted that, between 1985 and 1994, it aggressively marketed the synthetic hormone Protropin, one of its most lucrative prescription drugs, for various medical conditions for which the drug had not received Food and Drug Administration (FDA) approval. During this time period, the FDA had approved the drug only for use against a rare growth disorder found in a small percentage of children.

- As a result of an investigation in connection with a Qui Tam suit, a \$7,742,564 settlement was reached between the Government and the Chapter 11 trustee for the National Recovery Institute Group (NRIG). The suit alleged that NRIG, a drug and alcohol abuse clinic, billed TRICARE, Medicare and Medicaid for services not rendered in accordance with program requirements and for services that were not medically necessary.

- Investigation of a Qui Tam complaint resulted in a \$51 million civil settlement by Kimberly Home Healthcare, Incorporated, of Miami, Florida (Kimberly), a subsidiary of Olsten Health management Corporation. Kimberly pled guilty in U.S. District Courts in Atlanta, Miami and Tampa to assisting the Columbia Healthcare Corporation in the preparation and filing of false cost reports with the Government for home health care. In addition to the civil settlement mentioned above, the corporation was sentenced to pay fines totaling \$10,080,000.

- A \$4,149,555 settlement agreement was reached between the Government and Nova Southeastern University, Incorporated (Nova), Fort Lauderdale, Florida. The settlement was a result of an investigation into allegations that Nova billed TRICARE, Medicare and Medicaid for psychological services purportedly provided by licensed therapists or physicians when, in fact, the services at issue were provided by unlicensed student interns.

These are but a few examples of problems that pervade the health care industry and represent a growing challenge for the DOD.

Data integrity in management information systems has been a persistent problem affecting health care program effectiveness and efficiency. Incomplete and inaccurate data has made the DOD unable to clearly identify health care costs, identify unit and individual readiness for deployment, or coordinate direct health care with purchased health care. DOD management is now putting considerable emphasis on better data quality and significant progress is being made.

Transitioning to managed care is a critical element of peacetime health care delivery. The issue is complicated by a lack of understanding about TRICARE, multiple TRICARE programs offering similar but not identical benefits, and increased focus on providing peacetime health care to the growing retiree population. An audit of the TRICARE marketing program showed that while beneficiary understanding of TRICARE is improving, DOD has provided Service members with incomplete, incorrect, and inconsistent information. In addition, the combination of base and hospital closures and military downsizing, with a growing and aging population of retired beneficiaries (those eligible for Medicare but not DOD-purchased health care), more eligible veterans and their families are finding themselves without access to direct care resources. Attempts to address that problem have led to a proliferation of health care demonstration programs that have further confused the eligible population.

SUPPLY INVENTORY MANAGEMENT

Although DOD has substantially downsized its force structure, it has not reduced operations and support costs commensurately. However, the Department is pursuing over 300 logistics reform initiatives, many of which involve supply inventory management. The DOD intends to consolidate management of inventory functions and reduce warehousing requirements; reengineer DOD product support activities; adopt best business practices that include world-class standards of logistics performance; implement electronic commerce; and improve response times for delivering goods

and services to customers by expanding the use of prime vendors, virtual prime vendors, and direct vendor delivery. Determining appropriate requirements for materiel to be managed and stocked, identifying and canceling purchases of excess materiel, eliminating unnecessary items from inventory and distributing items more efficiently are areas that need improvement. In addition, spare parts shortages impacting readiness are being reported by operational units and repair depots, total asset visibility initiatives remain insufficient and inappropriate disposal practices continue to be a problem for the Department. Accordingly, supply inventory management remains a high risk area.

The Department has reduced wholesale supply stocks by almost one half over the last 10 years, from about \$107 billion in 1989 to a current estimate of \$55 billion. Nevertheless, an FY 1999 GAO report states that about 60 percent of the total on-hand secondary inventory in FY 1997 exceeded DOD requirements. The DOD disagrees with the GAO figure, but it is clear that further improvement is needed in inventory management. The gradual transition from just-in-case to just-in-time supply support practices is reducing logistics costs, but operating units and repair depots are raising concerns about spare parts shortages. All of the Services are reporting shortages, but the problem is most acute for Air Force aircraft, as reflected in mission capable rates that have declined to 73 percent. The DOD needs to do a better job of forecasting requirements, making smart procurement decisions to achieve economical order quantities, executing spare part budgets, reducing repair cycle times and implementing information systems that are crucial to effective and efficient inventory management.

The Department has vulnerabilities in preventing public access to live ammunition, explosives, and other dangerous residue cleared from military ranges. An IG, DOD, evaluation of the munitions disposal process led to multiple recommendations to the Department in September 1997 to tighten controls and improve procedures for clearing ranges and disposing of munitions. Although conditions at the ranges and in the disposal process warranted immediate attention, and the Secretary of Defense designated the handling of unexploded ordnance a material management control weakness in January 1999, the cognizant DOD level offices were still determining responsibility for issuing guidance in September 1999. Fortunately, ongoing follow-up indicates that many installations and commands are taking corrective action despite the continued lack of DOD guidance.

Although the wave of property disposal caused by force structure and inventory reductions in the early to mid-1990's has abated, somewhat, the DOD still has a high volume of widely dispersed disposal operations which continue to pose significant challenges. The Department's ongoing efforts to improve asset visibility and requirements determination should help minimize the instances of needed items being sent to disposal, but more effective demilitarization practices are needed. The Department has implemented some audit recommendations in this area, but is lagging behind on others. For example, in April 1997 we reported that no effective process existed for determining which of the hundreds of thousands of Government-owned property items and other materiel in contractor plants were munitions list items requiring demilitarization screening and special disposal instructions. Regulatory changes to address that problem are still incomplete.

This area also remains vulnerable to criminal schemes, as indicated by the 57 open Defense Criminal Investigative Service cases involving disposal activities as of September 30, 1999.

OTHER INFRASTRUCTURE ISSUES

In addition to adopting more modern and efficient supply processes, the DOD needs to improve a wide variety of other support activities to cut costs. These include maintenance, transportation and facilities functions. For purposes of this discussion, the facilities area includes base structure, military construction, real property operations and maintenance, and environmental cleanup. The common challenge in these areas is how to cut costs to reduce the current imbalance between DOD administrative and other support costs on the one hand, and modernization and operations requirements on the other.

Disagreements between the DOD and Congress about depot maintenance outsourcing remain a problem, but the Department has moved forward on numerous public/private partnering arrangements that are promising. The Services are also attempting to streamline maintenance operations at other levels and the weapon system acquisition process is now geared toward expanded contractor life cycle support, which should be more economical. The Department has additional opportunities for management improvement and efficiencies by consolidating requirements for maintenance and repair contracts, implementing better performance measures, re-

structuring and modernizing management information systems, better accounting for depot maintenance workloads, and collecting more reliable cost information.

Although worldwide transportation costs have dropped during the 1990's, DOD costs have not shown proportionate decreases. Numerous initiatives are under way to address that problem. These include implementing a commercial, off the shelf, on-line, freight management and payment system (Powertrack) to replace the enormously inefficient, paper intensive, transportation vendor pay practices that currently create serious vulnerability to fraud. The DOD pays \$650 million a year to freight forwarders and shippers. In the controversial area of household goods shipments, which cost an additional \$1.2 billion annually, three pilot reform programs are ongoing. We are auditing the Powertrack system effort and some aspects of the household goods pilot programs, at the request of DOD managers.

The DOD is still burdened with the cost of operating more bases than are needed to support the force structure; however, the Congress did not grant the DOD requests in the last two budgets for additional base realignment and closure authority. It is still likely that an agreement will be reached on more closures at some future date. In addition to eliminating underutilized installations, the DOD needs to keep working to avoid unnecessary facilities investments and stretch available construction dollars as far as possible. The DOD is also faced with heavy costs resulting from hazardous waste products from the maintenance, repair and disposal of many current weapon systems, as well as ground and water cleanup at active, closing and closed bases. The Department is putting considerable emphasis on cost containment in this area, but more needs to be done. As in other areas, the environmental management effort is also challenged by fraud.

READINESS

The difficulty of maintaining sufficient military readiness at constrained budget levels has been the subject of congressional hearings and public dialogue for the past several years. In addition to financial problems, the readiness posture is affected by the changing threat environment, which now includes bona fide information warfare threats and concerns about weapons of mass destruction in the hands of terrorists. However, increased operating tempo (OPTEMPO) has probably had the most significant impact on readiness, affecting mission-capable rates, personnel retention, spare parts availability, unit training, and operations and maintenance costs.

Since the end of the Cold War, the frequency of U.S. military involvement in operations other than war has increased, while force structure and military end-strength have been reduced. This OPTEMPO has adversely affected the combat capability of deployed units in Bosnia and Southwest Asia as well as some units that remain at home station, as they have to pick up the work of the deployed units while simultaneously supporting them with personnel, equipment and spare parts. Aircraft participating in deployments are being flown more hours than is the case during regular training missions. It is estimated that some wings are putting about 2 years worth of flying hours on aircraft in about 6 months during their Southwest Asia deployments. This accumulation of flying hours, combined with the age of some aircraft, has revealed atypical and unbudgeted wear and maintenance problems particularly on the F-15C and the A-10 aircraft. The pace of these deployments is also, at least in part, causing aircraft mission-capable rates to decline and the increased consumption of parts has exacerbated existing parts shortages, causing cannibalization rates to increase. The logistics problems affecting many units, especially in the Air Force, were discussed previously under Supply Inventory Management.

Training is a key factor in readiness. The Air Force in particular indicates that aircrew combat proficiency may be declining partly due to frequent and recurring deployments. F-15 and F-16 fighter squadron personnel, particularly those participating in Operation Southern Watch in Southwest Asia, frequently described their mostly routine missions as having little combat training value. For the Army, especially at battalion, brigade, and division levels, current peacekeeping operations detract from the Army's established training cycle to sustain highly trained and combat-ready teams. While in Bosnia, armored and mechanized infantry units generally do not conduct any armored maneuver operations and are relieved from tank and Bradley gunnery requirements. The inability to conduct needed training threatens skills which are extremely perishable. Returning units to their wartime mission capability levels during peacetime is also a problem, taking from several weeks for some support units to more than a year for some combat units. In addition, entire units are not always deployed. As a result of deploying partial units, the non-deployed portions lack the officers and senior noncommissioned officers needed to train more junior soldiers, cannot conduct training above the small unit and individ-

ual soldier level, and have to do not only their work but that of the deployed portion of the unit.

Accurate reporting of unit level readiness also remains a concern. The Global Status of Resources and Training System (GSORTS) indicates that the readiness of units engaged in these deployments in all of the Services has been adversely affected. These effects are particularly evident in the Army with lower unit level readiness ratings, although division level ratings have recently received much publicity. However, important information about a unit's condition is not always readily apparent in GSORTS and sometimes not reported at all. Actual unit conditions are masked by factors such as the counting of temporarily assigned personnel against wartime manning requirements, optimistically estimating training status, and inconsistent reporting.

Other readiness indicators, such as reported backlogs of equipment and real property for maintenance and repair, are notoriously unreliable. There is extensive activity under way to address those problems; however, audit and inspection coverage of these and other readiness issues has been very limited over the past couple years, partially due to the need to monitor Y2K conversion status.

TURBULENCE FROM CHANGE

There are high stakes involved in the DOD efforts to implement fundamental reform throughout the Department and, in all cases there is a need to push ahead vigorously and expeditiously. In fact, in most areas even more should be done. Nevertheless, it must be recognized that the nature, scope, and duration of the DOD reform effort create a number of significant management challenges in their own right. Those "change management challenges" include:

- maintaining high workforce morale and productivity;
- continuously retraining the workforce to ensure they have adequate command of constantly changing rules and processes;
- harmonizing the thousands of changes and initiatives so that they do not conflict with each other;
- measuring the results of each initiative and getting objective feedback to validate reported performance; and
- maintaining appropriate emphasis on internal controls and accountability.

These issues are particularly hard to deal with because they tend to cut across organizational and functional lines. We believe that much more needs to be done to focus on workforce hiring, training and retention, because even the best new procedure or process will fail without a well motivated, properly trained and adequately supported workforce. Our pending report on the DOD acquisition corps reductions will highlight the problems that result from cutting the workforce in half while workload remains relatively constant. We will also discuss the "greying" of the acquisition workforce and the very high attrition rates projected over the next few years. High turnover compounds the training problem. These kinds of issues undoubtedly apply to other sectors of the DOD workforce as well.

The problem of conflicting goals and inconsistent emphasis may be inevitable when so many initiatives are ongoing simultaneously. The DOD has realized that virtually all aspects of its operations involve multiple organizations and disciplines, so that unilateral attempts by individual managers to redesign processes are doomed to failure. The growth in the 1990's of problem solving initiatives with a more integrated, cross-cutting approach is one of the most positive trends that we have seen in the Department. However, more needs to be done. For example, the finance and acquisition communities appear to be moving in opposite directions on contractor pay. The finance community is attempting to improve controls over payments by taking measures like rejecting vouchers with remittance addresses that are not in the Central Contractor Registry and may be suspect. Some payments could be delayed, but vulnerability to fraud and error would be reduced. However, some DOD acquisition officials believe that payments to contractors are not being made promptly enough, and they advocate making payment without any attempt to match invoices to receiving documents. The Department generally resolves inconsistent guidance, but in the meantime the workforce cannot help but be somewhat unclear about DOD priorities.

Finally, we believe strongly that proper oversight is particularly useful and necessary during times of major changes. Identifying impediments to implementing new laws and policies, suggesting ways to fine tune initiatives to make them more effective, and providing objective feedback on whether intended results are being achieved are the kinds of valuable support that auditors can furnish. Perhaps the best recent example of such support was our massive audit effort to help the DOD implement its Y2K conversion plan. The Department has been very generous in its

positive comments on the important contribution that we were able to make to the DOD success in overcoming the difficult Y2K challenge.

Unfortunately, the resources allocated to the OIG, DOD, are not sufficient to enable comprehensive oversight in many areas. Between 1995 and 1999, funded IG, DOD, work-years were reduced by 26 percent, while mandated and requested workload simultaneously increased. The Department scaled back further major cuts that had been planned for FY 2000 through 2004, but it was very disappointing when the Congress cut our FY 2000 appropriation request. The combination of that reduction and the continuing need for full scale audit support of Y2K conversion has hampered our efforts to increase oversight coverage of the high risk areas that I have discussed in this statement. Most of the individual DOD process changes and new systems have not been audited and the results are either unknown or unverified.

SUMMARY

In summary, the DOD faces a wide array of formidable problems, many of which will require years of sustained effort to solve. We believe that the DOD audit and investigative communities play a vital role in identifying those problems, helping to fix them and verifying results. On the whole, DOD managers recognize and appreciate that role and we consider our working relationships with all major DOD components to be good.

This concludes my statement.

STATEMENT OF JUNE GIBBS BROWN

Ms. BROWN. Thank you, Mr. Chairman and committee members.

Everybody is concerned about fraud, waste and abuse in Medicare and Medicaid. And as they are all very aware, these are complex problems. There are no quick fixes. However, I think we are making excellent progress in these problem areas that undermine taxpayers' confidence in the system and, of course, take a great deal of money.

But it is no time for complacency. In just the last month, for instance, we have had two settlements; one was for \$486 million with Fresenius, which is a dialysis products and service company. They are repaying that \$486 million to the Government, and they have also agreed to withdraw a net of \$137 million more in denied claims that they had. In addition to that, we settled with Beverly Enterprises, the Nation's largest operator of nursing homes, for \$170 million. So we are bringing back huge amounts of money to the Government, and most of that goes back into the trust fund.

Much attention has been focused on the Medicare payment error rate, which we have now reported in each of the last of 3 years. It was, the first year, \$23.2 billion, which was mentioned by Mr. Walker, and then it dropped to \$10.6 billion less over the following 2 years. So we now have the 1998 amount as \$12.6 billion. That is in the area of fee-for-service payments in the Medicare system.

I would like to stress that while the error rate estimate may include some instances of fraud, it is primarily not a measurement of fraud. There are many things that could be fraud that would escape that particular analysis. The reasons for the errors in this audit are insufficient documentation, medically unnecessary services, incorrectly coded services, or things that were noncovered. We do catch some instances of fraud, but basically things like falsification of documents or illegal kickbacks would not be caught in this annual audit.

I want to commend you, Mr. Kasich, on the Balanced Budget Act, which I know you were so instrumental in implementing. That is saving the Government \$70 billion over 5 years in new procedures and conditions that the Department is implementing under that

act. These reforms have been deterring high levels of abuse, and we think Medicare still pays so much in some other areas, such as mental health service, rehabilitation services, medical equipment and supplies, home health, nursing facilities, prescription drugs, Medicare contractors, managed care and Medicaid. We are doing other work in those areas, and much of it is outlined in my written statement.

For example, one statistic you would be interested in is that in a five-State study of partial hospitalization, those are services for people with serious mental health problems, we found over 90 percent of the Medicare payments were for unallowable or highly questionable costs.

We recently replicated a review of Medicare home health payments in four of our most populated States, and we found that 19 percent of those payments were highly questionable or improper. That was an improvement because the previous study showed that 40 percent of those payments were improper. So we still have a lot of work to do in that area, but it is going in the right direction.

We still encounter problems with the financial management accounting procedures of Medicare contractors. These are contractors of HHS who pay the bills. We have had 13 of them with major settlements, one for \$140 million, that they had to repay the Government. So even in this area, there are problems. HCFA is limited and must use a very specific group of contractors, so they have very little flexibility on selecting new people for these arrangements.

Now, we have a lot of cooperation going on in the health care area, and I think it has really paid off and has allowed for these huge settlements and big reductions in the increase in the costs over government of Medicare. In 1998, for instance, we had only a 2.5-percent increase, and in 1999, we have actually had a 1-percent decrease in the cost of Medicare. This is unprecedented. Most analysts have said that the Department's attack on fraud, waste and abuse is partly responsible for this change.

We work a lot in prevention, as well, because we feel that just catching people and getting money back isn't going to solve the problems. So we have initiated a new approach to work closely with the health care industry. We are producing compliance guidance, special fraud alerts and advisory bulletins to help them know what we expect of them and how to comply with our programs.

We have had a hotline since 1997. It has received 900,000 calls. We are now receiving about 11,000 a week. That is allowing beneficiaries and people who are working in the industry to report to us things they consider questionable, and we are having great success with that.

In 1999, this multidimensional approach, working with others such as the Department of Defense, who also has health care concerns, we have had 303 health care convictions, 534 civil actions, almost 3,000 exclusions from Medicare and other health care programs, \$251.5 million in disallowances, over \$400 million of investigative receivables, and \$11.9 billion in savings. These savings were achieved through legislative and regulatory changes recommended by our office. Then with our partners, including the Congress, they have been implemented. \$369 million was actually

returned to the trust fund in 1999. \$4.7 million was recovered for the Federal share of Medicaid, and the rest went to the States.

So, in conclusion, I think that the new authorities we have and the new resources have paid off, but I am very concerned about deliberate fraud, which continues. Also, we have a criminal element that has entered into this system, and are doing a lot to counteract that, but it is still a great problem. We cannot put down our guard.

Thank you. I welcome your questions.

[The prepared statement of June Gibbs Brown follows:]

PREPARED STATEMENT OF HON. JUNE GIBBS BROWN, INSPECTOR GENERAL, U.S.
DEPARTMENT OF HEALTH AND HUMAN SERVICES

Good Morning, Mr. Chairman. I am June Gibbs Brown, Inspector General of the Department of Health and Human Services. I am here today to discuss some of the most significant issues that confront our Department, focusing my attention on the Medicare and Medicaid programs. These are complex problems relating to fraud, waste, and abuse that defy quick fixes and simplistic solutions. But failing to address them undermines the effectiveness of our programs, costs taxpayers billions in lost and wasted dollars, and deprives vulnerable beneficiaries of the care and support they need. I really want to stress to you today that we need to remain vigilant, on guard, and steadfast in our efforts to address these problems. While we have made excellent progress in recent years, this is no time for complacency, declaring victory, or relaxing our guard.

We need no further proof of this than the announcement last month of the largest health care settlement in the history of the country. Fresenius Medical Care, the world's largest provider of dialysis products and services, agreed to pay criminal and civil penalties of \$486 million to settle allegations of improper payments for nutritional therapy and laboratory tests for patients suffering from renal disease. The company has also agreed not to pursue approximately \$196 million in denied claims in return for a payment of \$59.1 million.

The progress we have made in the area of fraud, waste, and abuse is in large part because of the efforts of a wide variety of individuals and entities including the Department, the Congress, the Department of Justice, other law enforcement agencies, provider groups, and beneficiaries. These efforts have resulted in structural and payment reforms, heightened awareness, and prosecutions of wrongdoers. Much public attention has been focused on our Medicare error rate (which we have now reported in each of the last 3 years) and the fact that the projection dropped in half in FY 1998. While this has been extremely encouraging, the error rate is still too high, there are still particular areas of Medicare that are highly susceptible to fraud and abuse, and there are still daunting issues that confront us that are not reflected in the published Medicare error rate.

With respect to the last point, I would like to stress that while the error rate estimate may include some instances of fraud, it is a payment error estimate and not a fraud estimate. That is, since our review consisted primarily of a review of medical documentation, it is unlikely to detect all instances of fraud. The review would catch some instances of fraud such as where providers did not exist. However, it is less likely to detect more sophisticated fraud, such as falsification of documents and illegal kickbacks. Therefore, the true prevalence of fraud remains unknown, but based on other work we have done we believe that it remains substantial. We believe that we can make the most progress in combating fraud by continuing to focus our resources on specific areas of vulnerability rather than attempting a broad overall measurement of the prevalence of fraud.

With this in mind, I would like to spend my time with you today discussing the vulnerabilities that confront us, and some of our recent and ongoing initiatives.

BACKGROUND

The Office of Inspector General (OIG) was created in 1976 and is statutorily charged with protecting the integrity of our Department's programs, as well as promoting their economy, efficiency and effectiveness. The OIG meets this statutory mandate through a comprehensive program of audits, program evaluations, and investigations designed to improve the management of the Department and to protect its programs and beneficiaries from fraud, waste and abuse. Our role is to detect and prevent fraud and abuse, and to ensure that beneficiaries receive high quality, necessary services, at appropriate payment levels.

The Health Care Financing Administration (HCFA) is the largest single purchaser of health care in the world. With expenditures of approximately \$310 billion, assets of \$181 billion, and liabilities of \$40 billion, HCFA is also the largest component of the Department. Medicare and Medicaid outlays represent 34.2 cents of every dollar of health care spent in the United States in 1998. The Medicare program is inherently at high risk for payment errors due to its size as well as its complex reimbursement rules, and decentralized operations (39 million beneficiaries and 860 million claims processed annually).

OVERALL MEDICARE PAYMENT ERROR RATE

As part of our first comprehensive audit of HCFA's financial statements for FY 1996, we began reviewing claim expenditures and supporting medical records. Our primary objective was to determine whether services were (1) furnished by certified Medicare providers to eligible beneficiaries; (2) reimbursed by Medicare contractors in accordance with Medicare laws and regulations; and (3) medically necessary, accurately coded, and sufficiently documented in the beneficiaries' medical records.

For FY 1998, we projected that net improper payments totaled about \$12.6 billion nationwide, or about 7.1 percent of total Medicare fee-for-service benefit payments. The FY 1998 estimate is \$7.7 billion less than the FY 1997 estimate of \$20.3 billion, and \$10.6 billion less than the FY 1996 estimate of \$23.2 billion—a 45 percent drop.

As in past years, the improper payments include anything from inadvertent mistakes to outright fraud. We cannot quantify what portion of the error rate is attributable to fraud. We have, however, quantified the estimated provider billings for services that were insufficiently documented, medically unnecessary, incorrectly coded, or non-covered. These were the major error categories noted over the last 3 years. Some examples:

- Medicare paid a physician \$871 for 40 hospital visits. The medical records, however, supported only 18 visits. Therefore, payment of \$479 for the 22 visits without supporting documentation was denied.
- A community mental health center was paid \$21,421 for a beneficiary who received services under the "partial hospitalization" program. This program is limited to providing services to beneficiaries with very serious mental conditions that would otherwise require inpatient hospital stays. The medical reviewers determined that the beneficiary had already achieved sufficient stabilization and did not meet the definition of one who would otherwise require in-patient services.

SPECIFIC VULNERABILITIES CONFRONTING THE DEPARTMENT

While it is encouraging that the Medicare error rate overall has declined, the challenges and issues confronting the Department are still daunting. There are specific areas or pockets of the program that are particularly vulnerable to fraud and abuse or quality control problems. This may be due in part to inadequate enrollment procedures for providers, deficient internal controls, excessive payment rates, or especially vulnerable beneficiaries.

MENTAL HEALTH SERVICES

We continue to be concerned about inappropriate Medicare payments involving mental health services in a variety of settings.

- *Community Mental Health Centers.* In 1998, the OIG completed its five-State study of partial hospitalization services provided in community mental health centers and found that over 90 percent of the Medicare payments (\$229 million of \$252 million) were for unallowable or highly questionable services.

- *Hospital Outpatient Departments.* We are currently completing in-depth reviews of outpatient psychiatric services provided by 10 acute care hospitals. Also, a similar 10-State review and individual hospital audits of outpatient psychiatric services is being performed at psychiatric hospitals.

- *Mental Health Services in Nursing Homes and Ambulatory Care Settings.* In 1996, we examined the provision of mental health services to nursing facility residents. We found that for 32 percent of the records reviewed, Medicare paid for medically unnecessary mental health services in nursing homes. We are currently conducting a follow-up study. We are also conducting a similar study of mental health services in ambulatory care settings.

REHABILITATION SERVICES

The Medicare program provides coverage and payment for physical, occupational, and speech therapy services that are reasonable and necessary to treat an individual's illness or injury. These services are provided in a variety of settings, including

nursing homes, various rehabilitation facilities, and outpatient departments of hospitals.

- *Nursing Homes.* We found that 13 percent of physical and occupational therapy given to Medicare patients in nursing homes in 1998 was not medically necessary or was provided by individuals who did not have the proper qualifications to do so. The cost of these improper payments was \$1 billion.

- *Outpatient Rehabilitation Facilities.* The OIG has an ongoing six-State review of outpatient rehabilitation facilities in Florida, Louisiana, Michigan, New Jersey, Pennsylvania, and Texas, which accounted for about 50 percent of the total outpatient rehabilitation facility payments nationwide during CY 1997. Our results to date indicate that Medicare fiscal intermediaries may have made substantial payments for unallowable or highly questionable services.

We are continuing our studies of therapy services provided in nursing homes to ensure that waste and abuse are prevented while necessary services are rendered. Additionally, the OIG is currently planning a review of therapy services provided in outpatient departments of acute care hospitals. We will select a statistically valid sample of claims and request medical record reviews to determine whether the therapy services provided were reasonable and necessary for the patient's illness or injury.

MEDICAL EQUIPMENT AND SUPPLIES

While Medicare payments for medical equipment and supplies represent a small proportion of the program (about \$6 billion), over the years we have devoted significant resources to this area due to the significant problems associated with the provision of this benefit. We have consistently reported on excessive Medicare reimbursement rates, unnecessary services, services not rendered, and sham business billing Medicare. For example:

- We found that Medicare paid an estimated \$20.6 million in 1997 for services that started after a beneficiary's date of death. Almost half of this was for durable medical equipment claims.

- We recently reported that 42 percent of claims for orthotic body jackets were for more expensive items than the one actually provided. In a separate report, we found that Medicare pays substantially more for these items than Medicaid programs and other Federal payers that we reviewed.

- We reported that nearly 25 percent of certificates of medical necessity for home oxygen were inaccurate or incomplete. In addition, 13 percent of beneficiaries reported never using their portable oxygen systems.

- We found that 57 percent of documentation for therapeutic shoe claims were missing or inaccurate. Many recent reforms have been made in this area. For example, the Balanced Budget Act of 1997 requires providers to pay a modest surety bond. However, this provision has not yet been implemented. Furthermore, we believe that additional action should be taken to reduce payments for selected items, such as hospital beds, and that providers should be required to pay an application fee to cover the cost of processing their applications to participate in the program. Our work in this area continues with studies related to blood glucose test strips, ventilators, orthotics, and the National Supplier Clearinghouse.

HOME HEALTH

The 1990's saw dramatic increases in Medicare payments for home health services, growing from \$3 billion to almost \$18 billion during this period. Some of this growth was due to the legitimate need for and the value of these benefits for homebound Medicare beneficiaries. But, we also saw signs that fraud, waste, and abuse were significant contributors.

Based on our work, we found the home health benefit to be a program that grew too quickly with inadequate controls. The inability of Medicare to effectively identify improper claims before payment combined with the ease of entry of home health agencies into the program makes the Medicare trust fund especially vulnerable to losses from the home health program. For example, a 1997 audit disclosed that 40 percent of the claims sampled in four of the most populated States should not have been reimbursed.

Fortunately, most of the vulnerabilities have been addressed by the Balanced Budget Act of 1997 and in subsequent Department regulatory and administrative initiatives. These solutions are now being implemented through the development of a prospective payment system, increases in the number of audits, more thorough enrollment and re-enrollment procedures, and various new penalties for abusive actions. Additionally, as the home health agencies themselves are best positioned to guarantee the integrity of their product, we recently issued "Compliance Program

Guidance for Home Health Agencies” to assist them in developing specific measures to combat fraud, waste and abuse, as well as in establishing a culture of ethics that promotes prevention, detection, and resolution of instances of misconduct.

To determine whether these program changes were having a positive impact on Medicare reimbursement, we recently replicated our 4-State review. Our report revealed that the error rate had, in fact, been significantly reduced, down from 40 to 19 percent. Although this reduction indicates notable progress, a 19 percent error rate is still too high and we are still far from finished with the task of reforming the home health program. Until all the recent reforms are fully implemented, the Medicare home health program will remain a serious risk.

NURSING FACILITIES

We are continuing our longstanding monitoring of Medicare payments made on behalf of nursing home patients.

- *Infusion Therapy.* We recently reviewed infusion therapy services (such as use of an electronic pump to administer drugs) provided by some suppliers to skilled nursing facilities. Our audit found that suppliers charged excessive prices for infusion therapy, provided unnecessary services to patients, and improperly billed for services that the nursing facilities, in turn, misclassified on the Medicare cost reports. We are concerned not only about the financial effects of the overpayments we identified but also about overutilization and underutilization of therapy services.

- *Access.* We also studied the impact of the new nursing home prospective payment system on access to care. We found that Medicare patients are able to access care in skilled nursing facilities, particularly therapy patients. In fact, we found that it is easier to place Medicare therapy patients in nursing homes after the new payment system went into effect than before. On the other hand, patients requiring extensive services are more difficult to place under the new payment system.

PRESCRIPTION DRUGS

While Medicare does not pay for over-the-counter or many self-administered drugs, it does pay for certain categories of prescription drugs used by Medicare beneficiaries. Since 1992, Medicare outlays for prescription drugs have grown dramatically, increasing from \$663 million to \$2.3 billion in 1996. Prior to January 1, 1998, Medicare payments were based on “average wholesale prices (AWP)” which are mainly provided by manufacturers but bear little relationship to actual wholesale prices. Based on our work, we believe that Medicare continues to substantially overpay for these drugs. Legislative options include basing allowances on acquisition costs, mandating rebates, and permitting/requiring competitive bidding. We believe that such actions could save Medicare almost \$800 million annually, depending upon the option adopted.

MEDICARE CONTRACTORS

The Medicare program is administered by the Health Care Financing Administration (HCFA) with the help of 64 contractors that handle claims processing and administration. The contractors are responsible for paying health care providers for the services provided under Medicare fee-for-service, providing a full accounting of funds, and conducting activities designed to safeguard the program and its funds. There are two types of contractors—fiscal intermediaries and carriers. Intermediaries process claims filed under Part A of the Medicare program from institutions, such as hospitals and skilled nursing facilities; carriers process claims under Part B of the program from other health care providers such as physicians and medical equipment suppliers. We have encountered problems associated with:

- Financial management and accounting procedures and longstanding weaknesses in internal controls, including deficiencies related to the receivable amounts reported in HCFA’s financial statements and electronic data processing.

- The effectiveness of the Fraud Units which are designed to detect and deal with problems of fraud and abuse within the provider community.

In addition, there had been numerous allegations that contractors have falsified statements that specific work was performed, and altered, removed, concealed, and destroyed documents to improve their ratings on Medicare performance evaluations. Wrongdoing has been identified and we have entered into civil settlements with 13 Medicare contractors since 1993, with total settlements exceeding \$350 million.

MANAGED CARE

Managed care plans, such as managed care organizations (MCOs), provide comprehensive health services on a prepayment basis to enrolled individuals. Medicare beneficiaries have the option to enroll in these plans, which contract with HCFA to furnish all medically necessary services covered under the Medicare program. Medicare enrollment in managed care plans has been steadily increasing. In January 1993, 177 plans with Medicare contracts serviced 2.5 million beneficiaries. In October 1999, 409 plans had approximately 7 million Medicare enrollees. Medicare payments to managed care plans have also grown significantly—from \$8.6 billion in Fiscal Year (FY) 1993 to \$37.2 billion in FY 1999. Some of our most recent work includes the following:

- *Enhanced Payments to Managed Care Organizations.* Our past audits demonstrated that HCFA did not have effective controls over the higher capitation payments to MCOs for beneficiaries with either end stage renal disease (ESRD) or dually eligible (Medicare and Medicaid) status. These audits identified over \$122 million in improper payments. We have also been reviewing the extra payments made for beneficiaries with institutional status. Our audits indicate that there is potentially \$22 million in overpayments to MCOs for beneficiaries classified as institutional status. We are continuing our audits to identify overpayments based on institutional status at specific MCOs and also determining whether past problems with properly identifying ESRD and dually eligible beneficiaries have been corrected.

- *Fee-for-Service Payments to Disenrolled Beneficiaries.* The HCFA analysis of how well a MCO performs does not include reviewing fee-for-service (FFS) payments made for beneficiaries after they have disenrolled from the managed care organization. We identified \$224 million in Part A FFS medical services received within 3 months of the disenrollment date by these individuals. We are continuing our review to determine if the managed care organizations may have encouraged the disenrollment and/or provided poor care.

- *Administrative Costs.* Risk-based MCOs receive what appears to be a large amount of funds for administrative costs to operate their Medicare managed care programs. The HCFA has very little information available on how the MCOs use these funds, which are provided as part of the Medicare capitation amount. Based on our analysis of 9 MCOs, we found that the MCOs overestimated by 100 percent the funds they needed to cover administrative costs. We also found that the 9 MCOs had \$66 million in administrative costs that would have been disallowed had the MCOs been required to follow Medicare's general principle of paying only reasonable costs. We are also analyzing the variances in administrative funds (as a percentage of total funds received from Medicare) among MCOs.

- *Dissatisfaction of Vulnerable Beneficiaries.* Although beneficiaries, in responding to OIG surveys, reported generally positive experiences with HMOs, some indicated that they disenrolled because they received a lower standard of health care or because they felt their health had declined while in the HMO. This was particularly true of disabled beneficiaries and those with functional impairments and serious illnesses, who reported much less positively about their experiences.

MEDICAID

Medicaid is a means-tested health care entitlement program financed by States and the Federal Government—43 percent from the States and 57 percent from the Federal Government in FY 1998. To date, all 50 States, the District of Columbia, and the five territories have elected to establish Medicaid programs. The responsibility for detecting, investigating and prosecuting fraud and abuse in the Medicaid program is shared between the Federal and State Governments. Each State is required to have a program integrity unit dedicated to detecting and investigating suspected cases of Medicaid fraud. Most States fulfill this requirement by establishing a Medicaid Fraud Control Unit (MFCU). Although originally managed within HCFA, the oversight responsibilities for the fraud control units were transferred to our office in 1979 since the Units' activities were determined to be more closely related to the OIG investigative function. Federal funds for the Medicaid fraud control program are included in the Health Care Financing Administration appropriation. The program currently reimburses the States for the cost of operating a unit at a rate of 75 percent.

The types of fraudulent schemes we see in the Medicaid program in many ways mirror those in Medicare:

- *Billing for Services Not Provided.* This is one of the most common types of fraud. Examples include a provider who bills Medicaid for a treatment or procedure that was not actually performed, such as blood tests when no samples were drawn or x-rays that were not taken.

- *False Cost Reports.* A nursing home owner or hospital administrator may intentionally include inappropriate expenses not related to patient care on costs reports submitted to Medicaid.

- *Illegal Remunerations.* A provider (i.e., nursing home operator) may conspire with another health care provider (i.e., physician, ambulance company) to share a certain portion of the monetary reimbursement the health care provider receives (kickbacks) for services rendered to patients. Kickbacks include not only cash, but vacation trips, automobiles or other items. The practice results in unnecessary tests and services being performed for the purpose of generating additional income to both the referring source and the provider of the service.

In 1998, the MFCU reported 937 convictions and recoveries totaling more than \$83 million (Federal and State). It should be noted that there are areas of MFCU activity, such as patient abuse cases, that do not generate a monetary return, but are part of the overall effort to provide quality care and to hold the health care community accountable for the Federal and State dollars spent. In FY 1998, patient abuse cases accounted for over 30 percent of the 6,839 cases investigated by the 47 units.

Precisely because Medicaid is really a compilation of 56 separate programs, fraud and abuse coordination is extremely important. Therefore, the OIG, MFCUs, and other law enforcement agencies work together to coordinate anti-fraud efforts. For example:

- The OIG and MFCUs have joined with other State and Federal law enforcement agencies to organize health care fraud task forces throughout the country.

- The OIG has established with the Department of Justice and other enforcement agencies an Executive Level Working Group to focus on health care fraud.

- Ten years ago, the OIG helped establish the National Health Care Anti-Fraud Association, representing both governmental and private third party payers and law enforcement agencies, to coordinate governmental and private health care fraud enforcement activities.

Other cooperative efforts include State Medicaid Audit Partnerships. Five years ago, we began an initiative to work more closely with State auditors in reviewing the Medicaid program. The Partnership Plan was created as an effort to provide broader coverage of the Medicaid program by partnering with State auditors, 11 State Medicaid agencies and two State internal audit groups. Reports issued have resulted in identifying \$173.7 million in Federal and State savings. Since its inception in 1994, active partnerships have been developed in 23 States on such diverse issues as:

- Program issues related to Medicaid outpatient prescription drugs.
- Unbundling of clinical laboratory services.
- Outpatient non-physician services already included as an inpatient charge.
- Excessive costs related to hospital transfers.
- Excessive payments for durable medical equipment.
- Acquisition costs for Medicaid drugs.
- Program issues related to managed care.

Joint projects have also identified areas where improvements in program operations could be achieved, unallowable program expenditures could be recovered and future cost savings could be recognized.

WAYS TO ADDRESS THESE PROBLEMS

As noted earlier and as evidenced by the examples discussed above, the problems that I have discussed with you today are extremely complex. Clearly, the Department cannot eliminate the errors, waste, and fraud without relentless oversight through audits, investigations, and evaluations and through effective agency oversight. In the past, a stable source of funding was not always available. However, since the passage of the Health Insurance Portability and Accountability Act of 1996 our effectiveness has been strengthened through an increased and predictable funding base for us and the Health Care Financing Administration for fraud and abuse control efforts.

It became increasingly obvious that our traditional approaches alone would not be sufficient to win this battle. We needed structural reforms, new partnerships, and new ways of thinking. Only through a multifaceted, coordinated effort could we eliminate or mitigate the risks and avoid the consequences I have discussed here. Again, the Health Insurance Portability and Accountability Act of 1996 gave us the foundation for doing this. It authorized the Health Care Fraud and Abuse Control Program, a partnership between the Office of Inspector General and the Department of Justice to coordinate Federal, State, and local law enforcement activities with respect to health care fraud and abuse. We are very thankful that the Congress and

the Administration have provided us with additional resources and authorities in recent years to assist us in addressing the challenges we face. I would like to take a moment to describe some of the broad initiatives that we have taken as a result.

GENERAL UPGRADING OF CAPACITY

Our first step was to upgrade our facilities, methods, technologies, skills, and organizations. We are expanding our investigative efforts to new geographic areas, particularly in areas with higher than usual suspicious activity, and more generally in an all out effort to provide full security coverage for our programs. We have developed new analytic techniques and computing capacity to uncover and analyze suspicious payment and utilization trends which can then be investigated or audited as appropriate. We are combining our audit, investigative, evaluation, and legal functions to more effectively prevent, uncover, and respond to fraud and waste. And we have strengthened our procedures for coordinating our efforts with those of the Department of Justice.

In FY 1999 there were 401 convictions (303 were health care related), 541 civil actions (534 were health care related), 2,976 exclusions from the Medicare or other Federal health care programs, \$251.5 million in disallowances from questioned costs, and \$407.7 million in investigative receivables. The Office of Inspector General also conducted studies and made recommendations which contributed to the achievement of \$11.9 billion in savings related to program reforms and other actions to put funds to better use. Furthermore, \$369 million was returned to the Medicare trust funds in 1999, and an additional \$4.7 million was recovered as the Federal share of Medicaid restitution.

PROGRAM STRUCTURAL REFORM

It was clear that some of the more serious problems the Department was facing stemmed from the very structure of its programs. This was particularly true of those where payments to providers were based on their costs or charges. This approach contains inherent incentives to exaggerate prices and over-utilize services. Some programs also had very weak screening criteria and enrollment processes, enabling easy entry by unscrupulous individuals and business entities. Others used payment methods that made it too easy for Medicare to pay incorrectly in the first place and difficult to recover funds when improper payments were discovered. In many cases the sheer volume of payments made reasonable scrutiny practically impossible.

Examples of exactly these kinds of situations are those which I have described earlier in my testimony—including home health, nursing home, and mental health services, and medical equipment and supplies. No amount of auditing and investigating can adequately deter, detect, and respond to the errors, waste, and outright fraud that could occur in these areas. What is needed are fundamental reforms in the program structures themselves, and stronger safeguards in the form of certification standards and enrollment procedures.

We are particularly proud of the studies which my office contributed to promoting a greater understanding of the vulnerabilities that were addressed in the Balanced Budget Act of 1997. The Congressional Budget Office has estimated that the savings from the reforms to which we made contributions will total almost \$70 billion over 5 years.

FINANCIAL STATEMENT AUDIT

As required by the Government Management Reform Act of 1994, we issued our third comprehensive financial statement audit of HCFA. The purpose of financial statements is to provide a complete picture of agencies' financial operations, including what they own (assets), what they owe (liabilities), and how they spend taxpayer dollars. The purpose of our audit was to independently evaluate the statements and determine whether they were fairly presented.

We are pleased to report that HCFA has continued to successfully resolve many previously identified financial accounting problems. For example, substantial progress was made in improving Medicare and Medicaid accounts payable estimates, as well as estimates of potential improper payments included in cost reports of institutional providers. However, our opinion on the FY 1998 financial statements remains qualified. In accounting terms, a qualification indicates that we still found insufficient documentation to conclude on the fair presentation of all amounts reported.

Most significantly, Medicare accounts receivable (i.e., what providers owe to HCFA) were not adequately supported. We found deficiencies in nearly all facets of Medicare accounts receivable activity at the 12 contractors in our sample. Some con-

tractors were unable to support the beginning balances, others reported incorrect activity, including collections, and finally others were unable to reconcile their reported ending balances to subsidiary records. We also found that substantial amounts of receivables had been settled with insurance companies but were still presented as outstanding accounts receivable. As a result of these problems, we could not determine whether the Medicare contractors' accounts receivable balances and activities were fairly presented.

Material weaknesses are serious deficiencies in internal controls that could lead to material misstatements of amounts reported in the financial statements in subsequent years unless corrective actions are taken. The FY 1998 report on internal controls notes two material weaknesses besides accounts receivable:

- Financial reporting remained a material weakness because, among other things, HCFA does not have an integrated accounting system to capture expenditures at the Medicare contractor level. Instead, HCFA relies on a complex system of reporting that includes use of ad hoc reports to accumulate data for financial reporting.
- The HCFA central office and Medicare contractors continued to have material weaknesses in electronic data processing controls relating to security access, application development and change controls.

To ensure progress in reducing past problems while keeping abreast of continuing changes in the health care area and adequately safeguarding the Medicare Trust Fund, we recommended, among other things, that HCFA:

- Enhance prepayment and post payment controls by updating computer systems and related software technology to better avoid and detect improper Medicare payments and
- Continue to direct that the Medicare contractors and peer review organizations (PROs) expand provider training to (1) further emphasize the need to maintain medical records containing sufficient documentation, as well as to use proper procedure codes when billing Medicare, and (2) identify high-risk areas and reinstate selected surveillance initiatives, such as hospital readmission reviews and DRG coding reviews.

We believe these types of reviews are critical to reducing improper Medicare payments and ensuring continued provider integrity.

INDUSTRY OUTREACH AND EDUCATION

We have engaged in numerous proactive outreach efforts designed to help the medical care industry avoid fraud and waste, increase their compliance with Medicare rules, and generally understand more about the nature of waste, fraud, and abuse. Information about these outreach efforts and results of our audits, investigations, and evaluations are routinely made available through the Internet on our website at www.hhs.gov/progorg/oig. We have issued an open letter inviting health care providers to join us in a National campaign to eliminate fraud and abuse. Following is a brief description of these initiatives.

- *Compliance Guidance.* A cornerstone of our prevention efforts has been the development of compliance program guidance to encourage and assist the private health care industry to fight fraud and abuse. The guidance, developed in conjunction with the provider community, identifies steps that health care providers may voluntarily take to improve adherence to Medicare and Medicaid rules. Each guidance sets forth seven elements that we consider necessary for a comprehensive compliance program and identifies risk areas for the specific industry sector. So far we have issued compliance program guidance for use by clinical laboratories, hospitals, home health agencies and third party billers, hospices, durable medical equipment suppliers, and Medicare+Choice organizations. We also solicited input from the nursing home and physician communities on issues that should be addressed in upcoming guidance for those health care sectors.

- *Corporate Integrity Agreements.* Virtually all health care providers that enter into agreements with the government in settlement of potential liability for violations of the False Claims Act must also agree to adhere to a separate "corporate integrity agreement." Under such an agreement, the provider commits to establishing a compliance program or undertaking other specified steps to ensure their future compliance with Medicare and Medicaid rules. The duration of most corporate integrity agreements is 3 to 5 years, during which time the provider must submit an annual report to the OIG on its compliance activities. At the close of 1998, our office was monitoring 428 agreements; a total of 138 corporate integrity agreements were entered in 1999.

- *Special Fraud Alerts and Advisory Bulletins.* We issue special fraud alerts and advisory bulletins on topics that warrant attention by medical care providers. Through these publications we can spell out kinds of situations that could get pro-

viders into trouble. Recent topics include hospital payments to physicians to reduce or limit services to beneficiaries (commonly known as “gainsharing” arrangements); the effect of exclusion from Federal health care programs on excluded providers and those who employ or contract with them; and physician liability for certifications of medical necessity in the provision of medical equipment and home health services.

- *Advisory Opinions.* During this past year, in consultation with the Department of Justice, we finalized our process for providing written advisory opinions in response to requests for clarification from businesses regarding the sanction authorities enforced by the Office of Inspector General, including the anti-kickback statute and the Civil Monetary Penalties Law. From the inception of the advisory opinion program in February 1997 to the close of FY 1999, the OIG issued 32 advisory opinions. In addition, we frequently speak to industry groups on areas of suspected fraud and abuse and measures they can take to avoid trouble.

- *Self Disclosure Protocol.* Introduced as the Voluntary Disclosure Program as part of Operation Restore Trust, the self disclosure protocol allows health care providers to report questionable practices they discovered as part of a comprehensive compliance plan to the Government for resolution. The practices are more than simple errors that amount in direct overpayment to the contractors, but rather those issues that may be viewed as potential fraud and abuse. It allows the provider community to work with the Government in fighting fraud and abuse as partners instead of adversaries. The cooperative effort has created a better working relationship between the Government and the provider community regarding current health care fraud issues. We have had 70 self disclosures, 59 since our new protocol was published in the Federal Register in October 1998. To date, we have had 7 settlements amounting to \$4.3 million.

BENEFICIARY OUTREACH AND EDUCATION

Enlisting beneficiaries as partners in fighting fraud and waste assists in identifying abuses at an early stage, and preventing ongoing or widespread abuse. Our studies indicate that Medicare beneficiaries are well-positioned to identify possible fraud, with three out of four stating that they always read their Explanation of Medicare Benefits statements. We have been working with the Administration on Aging, HCFA, and AARP to carry out an outreach campaign to educate beneficiaries and those who work with the elderly to recognize potential fraud and abuse and to report it appropriately. State and local area offices on aging supported by the Administration on Aging have contributed to this effort. They are already teaching Medicare beneficiaries how to protect their Medicare cards and numbers, avoid situations which can lead to fraud, how to interpret their Medicare bills and explanations of benefits, and how to report questionable billings to Medicare or to the Inspector General’s Hotline.

Congress has also been of assistance in our fight against waste, fraud and abuse by enacting the Beneficiary Incentive Program in which individuals can receive cash awards in exchange for leads resulting in action against fraudulent or abusive providers.

FRAUD HOTLINE

In conjunction with both the industry and beneficiary outreach efforts, we have also been improving the toll-free hotline for beneficiaries and providers to report suspected fraud. Now millions of beneficiaries see the number 1-800-HHS-TIPS printed on the forms they receive that explain the Medicare benefits paid for them. Since 1997, the Hotline has received 900,000 calls which contributed to identifying \$30 million in improper Medicare payments, of which approximately \$6 million has already been recovered.

CONCLUSION

As I stated at the beginning of my testimony, I believe a concentrated effort by a large number of people has resulted in tangible progress in combating fraud, waste, and abuse in recent years. But as I have discussed with you today, the problems that remain are serious, complicated, and have profound consequences. I am particularly concerned about the deliberate fraud which we cannot always measure but that we know continues. We must never let down our guard, and we must continue to dedicate the resources and make the concerted effort to reduce these problems.

I really appreciate the opportunity you have given me today to focus attention on the continuing problems and vulnerabilities that confront us and to share with you some of our efforts and recent initiatives. I would be happy to answer any questions.

Chairman KASICH. Ms. Brown, let me just compliment you for your efforts to try to determine the number of the problems, try to measure the problems. I think you were the first one that actually pushed to have that done. I do want to tell you that I am glad those numbers have dropped. But I think those numbers dropping have been a matter of documentation, more than they have been systemic solutions, correct?

Ms. BROWN. Well, I would like to clarify that a little. When we have gone out for documentation of services, we would go out at least three times or four times to people, and they knew that they had to pay back if they didn't provide the documentation. It still didn't come in. I don't think it was a lack of good documentation. I think it was a lack of having provided the service, or knowing it was not a covered service, or something like that. Now we are getting the documentation in, and the errors also fall into other categories.

Chairman KASICH. But right now we are really virtually unable to—and I don't want to take away from the good work that has been done—it is kind of like, the reason I guess I am a little hesitant to talk to investigators and chide them at all, it is kind of like, well, we say we balanced the budget, and then they say, well, you idiots, you didn't pay down the debt. You know what I mean? So it is like it never ends. [Laughter.]

But I think we have to recognize up front that you have done good. And this is not designed to frustrate you or our friends that are here from the GAO, as long as a good effort is being made.

We really are virtually unable to do anything in Medicaid right now; is that correct? We haven't figured out how to do it.

Ms. BROWN. Well, we are doing some work in Medicaid. Three States are working with us to develop an error rate, but there are 56 different programs for Medicaid, and each one is individual. So they have to be done on a per-State basis. So North Carolina, Alabama, and Louisiana have been trying to develop that error rate, but they aren't there yet.

Chairman KASICH. So we really have 50 States that don't have an investigated system to check Medicaid.

Ms. BROWN. Well, not to check the error rate. But we work a lot in Medicaid. We have 23 different States that we are working jointly with to audit their systems and bring back money for both the State and the Federal Government. We provide the grants and oversee the Medicaid Fraud Control Units in each State. So those units also have significant work that they are doing strictly in the Medicaid area.

Chairman KASICH. Maybe we ought to ask them to give us a little bit more comprehensive work in Medicaid, Jim, so we can be more up-to-speed with what they are doing. In managed care, right now, we still don't have a very good measure for that, do we?

Ms. BROWN. No, we don't. We realize the vulnerabilities are almost the opposite type than we have in fee-for-service area, and we are doing some work in that area, but we haven't got the statistics on it.

Chairman KASICH. And in the fee-for-service area, there are a number of areas that you are unable to measure now; for example,

the creation of dummy practices and virtual patients; is that correct?

Ms. BROWN. Sometimes we catch it if the provider isn't legitimate. But we are doing more of that work through some of our other means. We have actually had, for instance, in Florida, a huge home health organization, and they have a room this size now that has documentation of patient records. Not one page of that is legitimate. They paid people to create those records, and they were getting millions of dollars from the Government for services that were never performed.

Chairman KASICH. It seems we have a system where we hand the checkbook to somebody to pay the bills, which is essentially what we have; is that correct?

Ms. BROWN. Yes.

Chairman KASICH. The pressure on them is to pay the bills so that they can get another contract to pay the bills. So it becomes very difficult. I have become pretty well convinced that in the area, particularly of Medicare, and there are a lot of problems, in terms of how you would make the transition, but until the buyer and the seller are together in this process, I am not convinced that we will ever fix this. And we really do not know the extent to which people waste money, take advantage of people, just simply in the area of coding.

Ms. BROWN. Yes.

Chairman KASICH. Or in the area of unnecessary services. But I think the good news is I think that the vast majority of physicians—I have never really met anybody in medicine that I consider to be dishonest, I really haven't. So I have got to think the numbers are small. But what you are talking about with that situation in Florida, you could get a whole con game going here in a lot of different ways, and it is hard to check because there is no "rubber meeting the road" in this.

Ms. BROWN. That is right. We have indicted 26 individuals there so far. Very, very few of the people are actually physicians or other health care professionals. We have another element that has moved in. As was brought out earlier, this is where the money is, so there are a lot of people who have no medical background that are arranging these very progressive schemes to bilk the systems.

Chairman KASICH. Mr. Mancuso, isn't the problem with not being able to do audits, that you have 2,000 years of supply of "X" in a warehouse somewhere, and it keeps getting ordered, and then you have real needs that are "Y," but we haven't ordered the parts because we ordered all of this "X," and we are not able to move the inventories properly and match the inventories with the legitimate needs? Is that not a pretty good analysis of what happens when you can't add up your books or keep track of your inventories?

Mr. MANCUSO. That is certainly a summary of an overall logistics problem, and it speaks to the Department's gradual move from "just in case" to "just in time"; meaning, moving from buying a lot of parts that you might need, to buying parts when you need them and having systems that can properly track them.

One of the things that we are watching in the Department and concerned about is last year, in the authorization act, the Congress required that the Department begin a very careful analysis of in-

ventory, a wall-to-wall inventory, and report back to the Congress later this year. We have seen virtually no movement toward complying with that.

On the other hand, there are some very positive things going on in the logistics area, as I had stated, about 300 different reform efforts that are ongoing. So there is certainly some progress, but much more needs to be done, and a lot of it is even tied in with the disposal problems that we have in actually disposing of some of the items in inventory.

Chairman KASICH. How long have you been over there?

Mr. MANCUSO. Since 1982.

Chairman KASICH. I came in, in 1983. Is there any way to fix this stuff?

Mr. MANCUSO. I would have to say that, from where we sit in the IG's office, there is progress, but it is never as fast as we want to see it happen. And there are a lot of competing interests within the Department; from warfighters who feel they have to have absolutely everything that they could possibly ever need on hand at any time, to people who are being more pragmatic and believing that they can develop a system that will be so precise that only exactly what you need would be available, and it would be available in a time frame that would work. The truth and the reality has to be somewhere in between. And what we have seen, again, is some significant progress, but it is a slow process. And it is better than it was in 1982, that is most certainly true.

Chairman KASICH. Is it an individual that can make a difference over there? You have to take a break from trying to deal with that building. Bill Owens left as the vice chairman of the Joint Chiefs because he was bashing his head up against the wall. It was hard for him to get the systemic changes he wanted. It takes so much effort to change. I know you need the systems, but even if you have somebody who is the head over there, it doesn't necessarily mean that the limbs are actually going to work because the head is making a command.

Mr. MANCUSO. That is correct.

Chairman KASICH. Do you just have to have a whole team of people that go in there? How, precisely, do you do it?

Mr. MANCUSO. I don't want to oversimplify, but there are several areas, where we feel a cross-cutting approach that had top-level management support would work. For instance, I think it was mentioned earlier, the Y2K conversion effort was something that the Department had not experienced before, where a single effort with a beginning and absolute ending date was designed. From the top levels of the Department, every manager was made to understand that they would, in fact, support this effort and be held accountable. In some cases, the Department spoke about withholding funds from managers who were not moving that process along.

We have recommended, and the Department has agreed, to apply the methodology that we devised during the Y2K conversion, toward tackling some of the larger problems in the Department. Although that idea has been accepted, we feel it is not moving along as rapidly as we would like to see it. We are concerned because the experience that people had in that effort is perishable. People come and people go. Right now there are a good number of people who

have seen how a cross-cutting, nonparochial effort can, in fact, work. We are hopeful that we will be able to apply this approach to a number of processes.

Chairman KASICH. I am going to get to Mr. Sununu who is going to talk about HUD, and Mr. Hoekstra about education, and I know that my colleagues on the other side will have a couple of questions.

One final question: Remember I mentioned about the bounty hunter? If you actually put a system into place that said that you save "X" dollars, you get a piece of it, what do you think would happen?

Mr. MANCUSO. There actually are a few systems in place that have been used, but not in a widespread way.

Chairman KASICH. I know that there are a few examples, because I have checked it—

Mr. MANCUSO. Well, for instance, the IGs—and many people are not aware of this—are actually able to award money to people within the Department who have managed to save money or to assist in matters that go beyond their normal call to duty. I have seen where that has happened. I have seen people in that area who worked with that person or people who now become more energized and a little more vigilant, and certainly it is a useful process. But, again, that is on a very small scale.

What you are suggesting is certainly something that is worth considering. The management of it, again, in a large department might be a bit difficult.

Chairman KASICH. You were shaking your head no, Ms. Gaffney. Is that a bad idea?

Ms. GAFFNEY. Yes, I think it is a bad idea.

Chairman KASICH. Why?

Ms. GAFFNEY. Oh, I think, you know what I was trying to say to you before about setting out certain performance indicators, standards: you start warping people's behavior. So, if you say you think I will respond to money, then pretty soon I am going to be getting that money however I can, even if it isn't the appropriate way. You have to be very careful about setting out those kind of standards.

But I would tell you, Mr. Kasich, our people, if you are talking about our agents and auditors, they are highly motivated and highly dedicated. They don't need more.

Mr. MANCUSO. I did not understand you to mean you were talking about the oversight people in the Department.

Chairman KASICH. I hope you are not broken down on the side of the road tonight and any of those people pass by, but nevertheless—

[Laughter.]

Chairman KASICH. Give me a call. I will come get you.

What did you say?

Mr. MANCUSO. I did not understand you to mean that you were talking about our auditors and investigators, but rather someone who may be buried in the logistics area, for instance, who might come up with a good idea.

Chairman KASICH. That is what I am saying. Look, I had a guy who worked in a—I don't need to tell you. We all have our stories. I don't need to tell you a story.

Yes, Ms. Brown.

Ms. BROWN. I was going to say there is the Qui Tam provision, which means essentially a whistle-blower can turn in information, ask the Government to join in. Essentially, they can sue.

In this case I mentioned, the whistle-blowers got over \$30 million.

Chairman KASICH. I saw that television show. And there was a big court case about who got what, wasn't there?

Ms. BROWN. Well, they always have—it is decided by the judge, and the amounts are usually 10 to 15 percent. Well, when we have these multimillion dollar settlements, those are very large payoffs. There is a whole Qui Tam bar that is set up and very active in the country because of the large amounts that people are paid.

Chairman KASICH. Mr. Moran, you are recognized.

Mr. MORAN. Thank you, Mr. Chairman.

Mr. Chairman, the reason that I made the point about the Education Department, I wanted to get some things on the record because I do think that there is another side or that the full story is not as negative as some of our friends and colleagues would suggest.

For example, in 1993, early 1993, there was a management reform study that detailed a real mess that the Clinton Administration, Secretary Riley, inherited. And since then, the default rate has dropped to less than half of what it was when they came into office. Did you know that, Mr. Chairman? It is down to the lowest default rate ever, 8.8 percent. It has never been that low. They doubled their collections on defaulted loans. They went from a billion to \$2.2 billion. They put together a performance-based organization, and it seems to be getting a better hold on their financial assistance programs. They go through the annual financial audit.

But what I think you would be most impressed at, and I know you are probably aware of this, but perhaps—

Chairman KASICH. I am easily impressed too.

[Laughter.]

Mr. MORAN. Well, good. Then you ought to be very impressed by the fact that they have one-third fewer employees than they did in 1980, despite the fact that there has been a doubling of the Education budget. And nearly a quarter of all of the Education Department employees are involved in investigating fraud and abuse.

Chairman KASICH. I just wanted to tell you, you know, I tried to run against—

Mr. MORAN. Are you impressed?

Chairman KASICH. Well, I wanted you to know I tried to run against Lamar, so—

Mr. MORAN. Yes. Oh, OK.

Chairman KASICH. But here is the only thing I wanted to ask and that is I think probably the single biggest reason why we have a lower default rate, and I don't know this, is that we finally began to handle the proprietary schools, which had an enormous default rate, I would think that is No. 1.

No. 2, is the direct loan program, which has been argued a winner. We don't know if it is a winner because that is a place where the Federal Government is making a loan, and we don't know what all of the costs are up front and, we don't know what the default rate is going to be in the back. So the direct loan program is something that can't be measured yet. But, hey, I want to tell you, if there is progress made here, I am glad..

Mr. MORAN. Yes.

Chairman KASICH. I mean, cutting the total number of employees there, I am thrilled.

Mr. MORAN. Yes. And they have eliminated—

Chairman KASICH. But I think they ought to be able to add their books up, don't you think?

Mr. MORAN. I think that would be laudable. [Laughter.]

But they have also eliminated a third of all of their regulations. You knew that, too, I know. So I am glad you gave me an opportunity to put that on the record.

Chairman KASICH. Jim, could I tell you honest to goodness—

Mr. MORAN. Yes.

Chairman KASICH. I am not doing this because I want to make Secretary Riley look bad.

Mr. MORAN. Yes.

Chairman KASICH. That is not my interest here. I don't care about that. I am leaving here, man. I don't want to make people look bad. And if they are doing good, we have got to tell them. Like the Customs, apparently, he is doing a good—a great job, fantastic, praise him.

But you want to talk about what is going on, how many billions of dollars did we spend on SDI, and what do we actually have to show for it? That was under, what, 12 years of Republicans. It doesn't matter to me who is there. Let us just make it work.

Mr. MORAN. I agree. With regard to the student aid, one thing that would be very helpful is coordination with the IRS. It seems to me that is essential. And here, it is not the Education Department. I understand it is the IRS. They want a change of the tax code before they move forward.

But anyway, let me get to some of the things on HUD. The HUD report is perhaps the most critical. I know that Secretary Cuomo is not 100-percent excited about all of your findings or perspective on this, Ms. Gaffney, but I do think there are a number of areas in HUD, where you are right on.

And I know, in terms of Section 8 subsidies, for example, we do have a long ways to go to fix some of the integral problems there. When you leave it up to the tenant to report their income, it is contrary to human nature not to give a figure that is going to ensure that they can keep an affordable house for their family. And I don't know a whole lot of families who are so conscientious that they don't underreport that income. I can understand why it happens, but I think we need stronger systems. And I am glad that you are suggesting that because it does deprive money from people who legitimately need it.

And I have to say, and I have worked with Mr. Lazio on this, 80 percent of the people who are eligible and who are not getting housing, generally speaking, there are far more compelling needs

within that four-fifths of the eligible population than there is within the people who are actually getting it. And I think we need to be tougher in terms of eligibility. And I suspect even the \$80 million is understated.

You can respond, and particularly if you disagree with anything I say, but I want to cover a few things. In terms of the Defense Department, we just came out of a hearing, military health care, lots of money. It is estimated that there may be a shortfall of over \$5 billion over the next 4 years in terms of the actual health care, military health care needs, even though there is a big increase in the budget. The DMARC came up with that estimate, apparently.

But there are a lot of areas where management reform would probably save tremendous sums of money. For example, have we ever done a survey, Mr. Mancuso, to give us a sense of how many people who have health insurance coverage go to military treatment facilities, get it for basically free, and don't use their other health insurance? For example, you have got an enormous population of people who retire after 20 years in the Service, but they are in their early 40s. Most of them move on to the private sector. They then vest, and they also become eligible, oftentimes, for a pretty decent health care plan.

If the military health plan is more generous and accessible, then they don't use that plan. And in some cases, I know a lot of consultants, they don't offer a health care plan to military retirees because the military retiree doesn't need it. So we are subsidizing their employer.

Has there ever been a study of that, the extent of duplication of coverage?

Mr. MANCUSO. No, not to my knowledge, Congressman. I do know that the people in Health Affairs who run the military program have looked at a number of different ways that they can find savings. One of the ways recently was to begin to coordinate with the Medicare program and have people, as they move into Medicare, fall into that system. I am not sure if you are aware, but there has been considerable outrage and much to be said about that effort. People feel, and it is just a commonly held belief, that if you enlist in the military, if you serve your 20 years, you should be entitled to that service, to military health care service, from cradle to grave, regardless of what other health insurance you might have or what other Government benefits might, in some way, substitute.

And, again, I don't feel I can speak more competently than that on this issue. It is not an area we have looked at, although I know it is an area that the people in Health Affairs have attempted to consider in their efforts to control costs.

Mr. MORAN. We have a lot of bills pending now that would provide universal full coverage to all military retirees. I think some form of audit to determine the amount of what really is, what is the term when you pay for something that is already paid for? You charge it to another firm, the States, we do that with new programs. It begins with an "S."

Mr. MANCUSO. Subrogation.

Mr. MORAN. I guess it is subroga—well, I am not sure, no.

Mr. MANCUSO. Insurance companies do it.

Mr. MORAN. But anyways, you know what I am talking about. And I think we are saving a lot of insurance firms that have been paid for that coverage lots of money by offering this, and we ought to look into that before we take on an immense new entitlement, as compelling as the needs may be in many cases.

I wanted to also, though, ask before my time is up, the base closings, can you give us a figure for how much potential savings has been lost because we have delayed the next round of BRAC?

Mr. MANCUSO. I can only repeat the Department's position. I believe the Secretary uses a figure of about \$3 billion a year that he would foresee in annual saving. Now, of course, during the course of our work we can see some of these areas where efficiencies could be had. So we have long supported the idea of continued base closings or a new base closure effort.

Mr. MORAN. Yes. I think more strongly than some of us in the Congress have, for obvious reasons, but it is a substantial amount of potential savings.

The last thing I want to say, it is not a question, Mr. Chairman, but you made the point that you don't know any dishonest doctors, and I may know a few, but not very many. [Laughter.]

But you have to ask yourself is it dishonest or simply good business practice when you provide a service that is marginally compensated, but that could be described as a service that is compensated at a much higher rate? And I don't know many doctors that don't pick the description of a medical service that has the highest compensation rate and charge Medicare that, rather than the lower. They do it to Medicare. They don't do it to HMOs because HMOs don't allow it. But many times if you take the actual described service, you will find that what was provided could have been charged, it could have been described as something else and charged at a much lower figure. And I think that is one of the things that is endemic within Medicare reimbursement, and I don't know how you get a handle on it. But I think it is substantial and serious.

Chairman KASICH. I think you have a situation today, where, Jim, I think that there is a doctor on this committee who said we always charged the lower rate because we didn't want to get caught charging the higher.

But I have a friend at home who now has a practice with a number of doctors in it, and they have a building, and he is a great friend of mine. And he said, you know, John, I just struggle to make sure that we don't fall to the temptation of coding at a higher level.

How do you ever get it done? That is our problem today, isn't it, trying to legislate ethics sometimes. So I think we can have some systems in place, but frankly, that is going to be their greatest challenge in the future; how do we get people to be just decent to one another.

Mr. MORAN. That is one of the more compelling reasons for managed care. Because when you do that, when you privatize it, there is an incentive to hold overall prices down, and particularly on a per-capita basis.

But thanks for the hearing, Mr. Chairman, and giving us the time.

Chairman KASICH. Mr. Hoekstra.

Mr. HOEKSTRA. I thank the Chairman.

Ms. Gaffney, thank you for, I read parts of your testimony, and thanks for putting it in perspective, saying you are dedicated and committed to the mission at HUD, and every time you find a dollar that could have been wasted or lost in fraud somewhere, you take that dollar and apply it to the other 20 or 30 percent of the people that can't access the services. I think we face much the same issue in any of the departments we deal with because the mission is very important.

I have got a couple of students here from my district, and when we lose a dollar or whatever in Education, it is Megan and Michael in the back or, in the future, to get the Chairman's attention, it is Reese or Emma that are going to lose the benefit of those dollars.

Just a couple of things, and before Jim leaves, in the supplemental that is going to come out in a couple of weeks, we are going to ask for some extra money to really go in and take a look at the financial systems and the expenditures within the Department of Education. I believe now we are out of four out of the five or we are approaching four out of five or five out of the last 6 years where the audits have been, from my perspective, less than acceptable. We are only one year where we have a clean audit.

The other thing, and I am sure Mr. Moran will agree with me on this, Jim, I am hoping that when we get back, I will have some legislation in place that will allow us to do the matching with the IRS and the student loans. And hopefully we can develop something that maybe we can do in a bipartisan way and get to the floor of the House and actually make it happen because I think we are all agreed on that.

Mr. MORAN. I would love to cosponsor like that.

Mr. HOEKSTRA. Right. Thank you.

Chairman KASICH. That would be a great thing; if as a result of Pete's work on his subcommittee and the work of this committee, that we could actually get that legislation done, get it written and get it to the floor like right away.

Mr. HOEKSTRA. Right.

Chairman KASICH. And I think we could do that. I think we could get it scheduled, but we need to know precisely what we need to write. But let's write it and do it, and let's try to get it done before we get to May.

Mr. HOEKSTRA. We will be working on that during the recess and, hopefully, get something—I think we all know what we want to get done. We have just got to get it written and make sure we write it technically in a correct way.

Ms. Lewis, you are going to come back, I think, to our committee on March 1. We are looking forward to getting the report from you. Number one, thank you for getting it done on time this year. Last year, having to wait 6½ or 8½ months past the due date just wasn't acceptable, and I am glad that you are going to meet your commitment that the report will be done.

I also appreciate you making available the auditors to meet with us this week to give us a preliminary indication as to what will be in that report. As I said a few minutes ago, I am disappointed with where we are, where the Department is, on being able to present

a clean audit. Obviously, they have made some progress. But the bottom line is that we are not getting a clean audit, and we are not getting a clean audit for an agency that has access or utilizes a lot of our dollars, a lot of the taxpayer dollars.

I want to ask some questions about information technology. I think in one of the documents that you sent to Mr. Armey, and maybe even to Mr. Kasich back in December, you had indicated that from 1995 through 1998 there had been like 115 recommendations, 88 of which remained open. And I think in testimony in front of our subcommittee back in December, you indicated that some of those were multiple or were—

Ms. LEWIS. Repeat.

Mr. HOEKSTRA. Were items that had been repeated.

Ms. LEWIS. Repeated, yes. I believe, Congressman, that was from the financial statement audits.

Mr. HOEKSTRA. Yes, I think that could be right.

In that process and in that tracking, was there a recommendation to begin a more accurate tracking of inventory of computer and electronic equipment, do you know?

Ms. LEWIS. I don't know, specifically. I can get back to you on that. I know, I recollect that there will be—I believe the matter has been addressed previously, either in the internal control report or the management letter. I believe it will be more specifically addressed in the fiscal year 1999 audit internal control reports due on March 1st.

In addition, this problem of a lack of good control over inventory has been self-reported by the Department in the annual FMFIA reports. What we have looked to do is bring some additional attention to this at the deputy secretary level to ensure that commitments made on paper to address these problems actually get followed through, and we are currently seeing some action.

RESPONSE TO QUESTION BY CONGRESSMAN HOEKSTRA CONCERNING INVENTORY OF
COMPUTER MATERIALS

OFFICE OF INSPECTOR GENERAL,
U.S. DEPARTMENT OF EDUCATION,
Washington, DC, March 6, 2000.

Hon. JOHN KASICH,
Chairman, House Budget Committee, House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: At the hearing on February 17, 2000, before your committee, I was asked a question by Congressman Hoekstra on an inventory of the computer materials in 1999. My response was "no." I would like to clarify my response for the hearing record. The Department collected data on information technology assets in 1999, including bar codes and physical descriptions of property on-hand. However, the inventory data was not complete and not fully validated by the Executive Officers of each of the principal office components of the Department. The Department also failed to review purchase orders to ensure that property that had been recently purchased was included in the inventory.

I request that this letter be included in the official hearing records of the Committee. If you have any questions, please feel free to contact me.

Sincerely,

LORRAINE LEWIS,
Inspector General.

Mr. HOEKSTRA. Yes, I am interested in that. When you communicate with the deputy secretary or the secretary, what are the different levels of communications that you have? I mean, sure there's

the informal, but there are written correspondence. What does it mean when you do a formal report?

Ms. LEWIS. A formal audit?

Mr. HOEKSTRA. A formal report. Is that a term that you use, that there may or may not be a formal report to the deputy secretary?

Ms. LEWIS. I can tell you that what I have seen since I have been there in June, and going back to look at some of our historical documents, is we have sent memoranda to the deputy secretary and Secretary on occasion. We have provided them copies of our audit report. Sometimes they are—

Mr. HOEKSTRA. So there is no such designation as a “formal report” that you are aware of? No. OK. That is all right.

Ms. LEWIS. I will have to go back and check and see if I have missed something.

Mr. HOEKSTRA. Was there an inventory of the computer materials and those types of things in 1999 that you are aware of?

Ms. LEWIS. No.

Mr. HOEKSTRA. There was not?

Ms. LEWIS. I am not aware of that. I am aware of the issue of the need for an inventory was reported on the 1999 FMFIA report.

Mr. HOEKSTRA. Do you know whether they conduct or, on a regular basis, conduct inventories of their computer and electronic equipment or not?

Ms. LEWIS. This is an area that we, in the OIG, are currently looking at very closely. I have asked the deputy inspector general to lead an effort to identify, from the past work we have done, very specific action items that the Department should be taking right now and forwarding those pieces of information to the deputy secretary, in addition to assisting the Department in whatever we can in terms of getting a better handle on its inventory control.

Mr. HOEKSTRA. You are aware that there may be a problem and there may be missing equipment?

Ms. LEWIS. I believe there is a problem, and it requires serious attention in the Department.

Mr. HOEKSTRA. Like I said, I think our focus is going to be on either getting to you or getting to GAO the resources necessary to get the financial controls in place at the Education Department. I think, with what we heard in the hearing in December, what we are going to hear over the next couple of weeks about the financial controls and the financial reporting, and with some of the other problems that are being brought to our attention within the Department, I would almost see it as a need for crisis management.

We are investing \$35 billion discretionary, \$50 to \$60 billion through the loan program in perhaps some of the most important spending that we have in Washington today, that is in the educating of our kids. And we can't continue to have this Department perform in the way that it is performing because this is just telling us where the money is going. And we can't even do that. And I think in some cases we are finding that it is vanishing in some very interesting ways. So right now we can't even say where the money is going.

And we really need to be focusing on the next issue, which is, OK, we figured out where the money is going, now is it actually making a difference? And when you don't know where the money

is going and where you can't track the money, you can't tell whether it is making a difference. Is it four out of the five or five out of the last 6 years that we haven't had a clean audit?

Ms. LEWIS. Four out of the last five have not been clean. 1997 was clean, and 1999 is expected to be four qualified opinions, plus one disclaimer on one statement.

Mr. HOEKSTRA. As I said earlier, for the layperson who hears qualified opinion, for the auditors, they said this is a C minus to a D minus, and when you are making the adjustments, compared to the \$1.7 trillion in the Department of Defense, that may be pretty good. But if you are comparing it to what is going on in the private sector, a C minus to a D minus, the auditors are telling you the trading of the stock would be suspended, and there would be an investigation. That is not good enough.

It maybe is not technically correct. I am not an auditor. I call it another failed audit because the auditors are saying, and the public in the private world, this stock in this company would be in big trouble. And that is why I refer to this as it is time to view this as a crisis because of the dollars that are going into this area and because of the issue that we are dealing with. Every dollar is important.

But when we are spending and committing it to our kids, and the parties are tripping over each other to see who can pour more money into that department and invest it on our kids and say, "Look, now, we are spending more than you are." "No, we have got more than you do," and all we are doing is we are pouring it into a Department that can't tell us really how much we are spending or where we are spending it is unacceptable. I am hoping that by putting the extra money through GAO, by recognizing that it is a situation for crisis management, maybe we will get the attention of the Department that they will actually focus on it and get it done because it has to happen, and it has to happen sooner rather than later.

Thank you.

Chairman KASICH. Mr. Markey, do you want to go now or do you want to—the gentleman is recognized.

Mr. MARKEY. Thank you, Mr. Chairman.

Ms. Gaffney, it is not your job to celebrate successes. That is not what we are doing here today. But upon reading your testimony, I am puzzled by your taking HUD to task for spending \$2 million on a contractor to get the books balanced, and you lead off your testimony with that expenditure.

HUD has been properly criticized over the years for not being able to balance its books. That has been a historical problem. Secretary Cuomo appears to have decided, perhaps out of frustration with the history of HUD, to stop trying to run a large cabinet agency without knowing where the money went, get a baseline. What is going on? Why have there been so many problems in the past?

An IG should be praising, Ms. Gaffney, that kind of intolerance of sloppy bookkeeping, not leading off your testimony with slamming him for it.

Now, I am gravely puzzled by a very disturbing trend within your own office with regard to making cash recoveries. In the last 5 years, the total cost savings and cash recoveries reported by the

IG's office at HUD has fallen from \$262 million in 1994 to \$78 million in 1999. There has been, in other words, a 70 percent decline in this recovery activity in your office during the time of your tenure. That activity seems to have collapsed on your beat.

Now, often we can blame that kind of collapse on a small office losing key staff, but in your case, the IG's budget at HUD has risen dramatically over the same period from \$46 million in 1994 to \$81 million in 1999, which is a 76 percent increase in your budget over the same time period that there has been a 70 percent decline from a peak in 1994 down to 1999.

In fact, in 1999, those two lines cross for the first time in history. That is, for the first time, the IG spent more money than it recovered at HUD, the law of diminishing returns having set in.

Put another way, while previous IGs recovered \$5 to \$6 for every dollar spent, your semiannual report to Congress shows that this ratio has fallen from 5-to-1 in 1994 to 3-to-1 in 1995 to 2-to-1 in 1997 to 1.5-to-1 in 1998 to less than 1-to-1 in 1999.

Now, I want to place this chart in the record, if I may, Mr. Chairman.

Chairman KASICH. I am impressed with all your investigative research here on the IG.

[The information of Congressman Edward Markey follows:]

HUD INSPECTOR GENERAL

[Dollars in thousands]

Fiscal year	Inspector General's budget, appropriated level	Inspector General's reported total cost savings and cash recovery ¹
1989	\$26,011	² \$177,355
1990	30,028	192,890
1991	38,804	262,964
1992	44,665	229,159
1993	46,160	250,846
1994	46,305	262,359
1995	47,356	121,462
1996	47,850	122,213
1997	52,850	82,832
1998	66,394	91,382
1999	81,910	77,897

¹ Derived from Profiles of Performance included in the Inspector General's Semi-Annual Reports to Congress. Figures include cash recoveries, savings, cost efficiencies realized, commitments to recover funds, cost efficiencies sustained, and fines levied. Prior to 1994, figures may include amounts due to HUD program participants.

² Prior to 1989, the IG did not report cost efficiencies realized.

Mr. MARKEY. I think that you have conducted yourself, Mr. Chairman, in a way that has inspired the rest of us. [Laughter.] Chairman KASICH. Thank you.

Mr. MARKEY. To the same kind of green eyeshades, bigger, and looking at this hearing the way you would want us to.

Ms. Gaffney, a cynic might conclude that we can't afford to keep you at work with that declining ratio. Now, if things don't change fast, your own management of the IG's office will become a major problem in and of itself. So how do you account for your record of now spending more money but recovering less? And what do you intend on doing on reversing that collapse?

Ms. GAFFNEY. Mr. Markey, before I answer that question, could I go to your first point, please, about the \$2 million?

Mr. MARKEY. Oh, please.

Ms. GAFFNEY. What we are all hoping for is that we will have financial systems that will generate financial statements that will be auditable. Yes, it is wonderful—and if I didn't say it—that people now care about getting unqualified opinions, about putting together financial statements. That is wonderful. But if you have to do manual work and hire contractors to put those statements together instead of getting them from your financial systems, the problem with that is you can't be sure that you are going to get an unqualified opinion the next year.

So the focus long term needs to be getting your financial systems in shape. Those financial systems are still not in shape at HUD, and that is what my point is, that that is what we need to work on. That needs—

Mr. MARKEY. Do you have a problem in getting a baseline number and spending—

Ms. GAFFNEY. Yes.

Mr. MARKEY [continuing]. And spending a relatively small percentage of the budget in order to start all over? You have a problem—

Ms. GAFFNEY. Mr. Markey, let me explain to you the current situation at HUD. This year HUD implemented a new core accounting system. It has been unable to maintain connectivity across the board with the feeder systems in HUD.

HUD didn't used to have one standard general ledger. This was a wonderful chance, a wonderful effort to develop one standard general ledger in HUD.

It has been difficult. The feeder systems aren't compatible with the new standard general ledger. So what has happened now is that they can't even post transaction changes in the standard general ledger to get financial statements. They are being posted in an entirely different system.

Am I making myself clear?

Mr. MARKEY. No, you are not. You are not. Not in terms of—you know, let me tell you this, OK? One of the things that this Budget Committee has on an ongoing basis is the difficulty of getting honest numbers. This committee has the highest percentage of—the highest prevarication coefficient in testimony before this committee than any other committee in terms of the numbers. So I personally believe that if a Cabinet Secretary says let's go back and examine all these premises from the past, let's get a zero-based budgeting here and start all over again, yes, there is going to be some discombobulation at the get-go. But in setting up that new system, setting up that tougher accountability, obviously you are trying to jar loose a lot of the bureaucratic inertia which has been in place over the years.

You know, we can disagree on this, OK? But I just think your focusing on a \$2 million expenditure at the lead-off of your testimony is—you know, there is a bit of—I don't know. There is a bit of snideness in the testimony, but—

Ms. GAFFNEY. I didn't intend that.

Mr. MARKEY. I know that, but it comes through. And I just—my time is going to run out.

Chairman KASICH. No, it isn't going to run out. Ed, would you yield for a second? I think what the gentle lady is trying to say is

that—and she is talking in a language of an accountant. What she is trying to say is she would like the people at HUD to be able to add their own books and make the numbers add up.

Ms. GAFFNEY. Right.

Chairman KASICH. That is what she is saying. She is saying she doesn't understand why we have got to hire somebody out here to decide what is going on in their own business. That is what she was saying about the \$2 million.

Mr. MARKEY. No, I appreciate that.

Chairman KASICH. And I would think you would want them to be able to reconcile their numbers.

Mr. MARKEY. I would want them to. I guess my point is that the agency was trying to accomplish a good purpose. The purpose was—

Ms. GAFFNEY. I agree with—

Mr. MARKEY [continuing]. To make the agency more accountable, to begin a process by which somebody is coming in from the outside and bringing all these internal parties that are inside the bureaucracy at HUD, bringing them together and trying to make some rational sense out of after a generation of bitter criticism of HUD being an inefficiently managed agency. I am saying that in doing that, that is something to be praised.

Ms. GAFFNEY. And there were days—

Chairman KASICH. She did say earlier—

Ms. GAFFNEY. There were years when Cabinet agencies didn't care whether they were able to produce financial statements.

Chairman KASICH. It is just curious to me that we have only picked on one IG since we have come in this room today.

Mr. MARKEY. How much time do I have? [Laughter.]

Chairman KASICH. But, wait, let me just tell you—but we have only picked on one, Ed. It is curious to me. It is fair to ask them the tough questions, also, but we have only picked on one.

The other thing that I wanted to say to you is—

Mr. MARKEY. She may have an explanation. Why don't you give her—she hasn't even had a chance yet, John, to give her explanation.

Chairman KASICH. Ed, I am not trying—

Ms. GAFFNEY. I would like to do that.

Mr. MARKEY. She may have a legitimate explanation. You are defending someone before she has explained—

Chairman KASICH. I am not defending her. I just don't want you to badger the witness. That is all.

Mr. MARKEY. I appreciate that.

Chairman KASICH. The only thing I am saying about what she said earlier—I wanted to explain to you—is she said with the items that Secretary Cuomo has put in place, she would hate for somebody to come in and dismantle them just because it happens to be, you know, a Cabinet Secretary who happens to be a Democrat. She was pleading for consistency in the next HUD Secretary.

Look, I don't want to get in the middle. I just don't like to see anybody get—I mean, you are doing fine. And Secretary Cuomo has just called me, and we are working together on a major item that I am very happy about. The gentleman has got his time.

Mr. MARKEY. OK. Could you answer the second part of the question?

Ms. GAFFNEY. Yes, Mr. Markey. I have our recovery numbers going back to 1992 through 1999. They do not resemble yours, so I don't know what your chart is, but let me read them across.

Mr. MARKEY. I am using the numbers that are derived from the profiles of performance included in the inspector general's semi-annual reports—

Ms. GAFFNEY. So am I.

Mr. MARKEY [continuing]. To Congress from your office.

Ms. GAFFNEY. So am I.

Mr. MARKEY. OK.

Ms. GAFFNEY. In 1992, the total recoveries were \$49 million. In 1999, they were \$48 million. In the middle years, they went as high as 73, 59.

Two things you need to know—three things. First of all, in 1992 and 1993, there were major—

Mr. MARKEY. Excuse me. I am sorry.

Ms. GAFFNEY. In 1992 and 1993, there were major reporting errors. I wasn't in the HUD OIG at that point, but there was \$40 million that was included in the recovery numbers in 1992 that shouldn't have been, \$14 million in 1993.

Nonetheless, your point is well made. Our budget has increased over this period, and what I am saying to you is that the recoveries have remained pretty static. And you are right to ask for an explanation. There is one big explanation: that is, when I went to the HUD OIG, I said I don't care about numbers. What I care about is quality work and having a positive impact on HUD.

The reason I said that, Mr. Markey, is all of the IGs during the late 1980s and the early 1990s were engaged in what I considered a pretty counterproductive effort. They had accepted dollar recoveries as the one measure of performance for IGs, and it is what I tried to say to you before. People aren't dumb. If I say to you give me numbers, you will give me numbers, OK, and you will fabricate—well, that is too strong a word. However, I really think that our focus should not be on generating that kind of numbers but on solid, substantive work.

Mr. MARKEY. Good. Thank you. And that is a fair answer. That is a very fair answer. Thank you.

Ms. GAFFNEY. Thank you.

Mr. MARKEY. OK. Thank you, Mr. Chairman.

Chairman KASICH. Thank you, Mr. Markey.

The gentleman from New Hampshire.

Mr. SUNUNU. Thank you, Mr. Chairman.

As always, somehow fate conspires to place me after Mr. Markey, and as always, I have drawn yet another kernel of knowledge from his wisdom: prevarication coefficient. I will remember that phrase, that fabulous metric by which we should measure the performance of all of our committees. Thank you, Mr. Markey, and thank you, Mr. Chairman—

Mr. MARKEY. Will you yield just briefly? Can I tell you where we got it from? When I was running for State representative the first time—

Mr. SUNUNU. I thought you just made it up on the spot.

Mr. MARKEY. No, no. When I was running for State representative for the first time in 1972 and all I had were my two brothers, so the three of us were ringing doorbells. And after about a month, we decided that we had won because everyone was telling us that they were with us at the doors that we were ringing.

So then finally one night we decided to build in a prevarication coefficient: How many people were actually telling us the truth or just being nice to the young men ringing the doorbells so that they wouldn't go away disappointed? So we decided it was about a one-third prevarication coefficient at the doors. So we had to actually increase our work rather than reduce it.

Mr. SUNUNU. Well, maybe the 33 percent will be our threshold for this committee from now on.

Let me offer a comment in response to the point that Mr. Markey made, and I think that the inspector general's response was certainly appropriate and giving credit for spending the \$2 million to have good books. But my experience is that there is a fundamental reason for being concerned about that, and that is because if you don't have the financial systems in place that give you that unqualified opinion, you may spend the \$2 million to know where you are, but the financial systems will have no ability to provide for improvement. So that you may know where you are, but you don't have good enough financial systems to bring down or to avoid the \$1 billion in fraudulent Section 8 payments that are described in the material that we were provided with. You don't have financial systems in place that are going to do anything about increases in FHA default rates or in poor performance in collecting bad debt.

If you want to improve in those areas, you are going to need the kind of financial systems in place that can give you the unqualified audit without spending the \$2 million.

So while I would agree with the point the gentleman made that it is certainly an achievement to have the audit in place, unless the systems are better we are not going to be able to make any material improvement.

I would like to ask Inspector General Gaffney to comment on a few other points that I had a chance to raise with the Comptroller General.

First, you said in a report you did in March of 1999, or I guess it was testimony before the Banking Committee, that you weren't able to reach any conclusions about the 2020 reforms. My question is: Since then, over the last year, have you been able to gather evidence or seen anything that would allow you to make a more specific qualification of what has or hasn't been successful in those reforms?

Ms. GAFFNEY. First of all, the position that HUD is in, you know, is that it downsized very severely, and then it scrambled to come up with ways to compensate for the downsizing. At this point, I think you could say that the single-family property disposition situation is certainly not in good shape. The 2020 response to downsizing the single-family staff was management and marketing contractors. Then we had the InTown debacle.

Right now the inventory is higher than it was when we started those contracts. More importantly, it is aging significantly, and you know the impact that that has on neighborhoods.

I believe HUD has a problem with contract administration. Eventually, I sincerely hope it will get its act together and this will work.

Mr. SUNUNU. Is poor contract administration the single biggest reason for the deterioration in the FHA portfolio, the HUD-owned properties?

Ms. GAFFNEY. At this point, I don't have enough information about all the management and marketing contracts, but InTown was the major influence in that buildup of the inventory.

Now, HUD terminated that contract in September, but by that time InTown had disposed of almost no property at all.

Mr. SUNUNU. Has anything—

Ms. GAFFNEY. And that wasn't a contract administration problem. They knew, HUD knew what was going on. But the award of that contract was problematic.

That contract covered 40 percent of our REO properties, and OIG auditors could find no evidence that HUD looked at InTown's financial capability.

Mr. SUNUNU. It seems to me to be quite counterintuitive that this portfolio would deteriorate—would expand and grow at a time when economic prosperity around the country would seem to create the most favorable possible climate for disposition.

Ms. GAFFNEY. Right.

Mr. SUNUNU. What other causes could there be for such deterioration?

Ms. GAFFNEY. The major cause, in the last 10 months, the last year, has been InTown Management, which simply did not perform at all. Prior to that, the inventory had been increasing, and our auditors attributed it to the severe cuts in single-family staffing. And their finding was, when—

Mr. SUNUNU. What was the reduction in staffing?

Ms. GAFFNEY. It was cut in half, from about 2,000 to 1,000. And what the auditors further found was that in HUD, if it is a choice between doing something that generates more business or taking care of business on hand, it is the new business that takes priority.

So, for instance, if you have a choice between using scarce staff to do more insurance or to take care of this inventory of REO, you choose to generate more insurance.

Mr. SUNUNU. What are they doing now? InTown went bankrupt in September, correct?

Ms. GAFFNEY. They redistributed the InTown—

Mr. SUNUNU. Has any progress been made in the last 6 months?

Ms. GAFFNEY. I think in the last 2 or 3 months or perhaps 4 or 5, the inventory hit a high of about 52,000. It is down to 47,000. So that is good news. The bad news is that every single month over the last year the percentage of properties over 6 months old and over 12 months old has increased, and that is through January 30.

Mr. SUNUNU. Well, it would seem to me that has little or nothing to do with InTown, then, or with the bankruptcy, that there is obviously far more fundamental problems than just the contract management.

Ms. GAFFNEY. Well, it would seem to me that the contractors are finding it in their interest to under the cream of the crop, that is,

houses newly coming into the inventory, rather than deal with the old stuff that has been sitting around for a long time.

Mr. SUNUNU. What other reforms have been suggested or initiated in the past 3 or 4 months?

Ms. GAFFNEY. In the past 3 or 4 months, HUD has done an income match. That is the income verification issue.

Mr. SUNUNU. What does "just currently" mean?

Ms. GAFFNEY. In September, I think they did the first ever broad income match. And just yesterday they started sending out 280,000 letters to residents notifying them that it appears that you have underreported your income by significant amounts.

Mr. SUNUNU. Notwithstanding the timeliness of that initiative, has anything been undertaken before to try to deal with the problem of underreporting income?

Ms. GAFFNEY. Over the years, they have done a variety of pilots. Every year we do a sample for the purpose of the financial statements.

Mr. SUNUNU. Is there a systemwide methodology used for income verification?

Ms. GAFFNEY. They are proposing a systemwide methodology for—

Mr. SUNUNU. But there is not one now—

Ms. GAFFNEY [continuing]. The first time. Well, we are starting down that road for the first time.

Mr. SUNUNU. How is income verification done currently, then? Is it just inquiry, through the application process? They ask "what is your income," and you write it down on the form.

Ms. GAFFNEY. Right, and—yes.

Mr. SUNUNU. But there is no—

Ms. GAFFNEY. Systematic way—

Mr. SUNUNU [continuing]. Formal system or—

Ms. GAFFNEY. Right.

Mr. SUNUNU [continuing]. Where there is a verification process through an employer?

Ms. GAFFNEY. There has not been, no.

Mr. SUNUNU. At the local level, is there ever an effort to verify income through an employer?

Ms. GAFFNEY. They are supposed to be doing that at the initial screening.

Mr. SUNUNU. But there is no process, no HUD-driven process, to verify income?

Ms. GAFFNEY. No, has not been. There is now.

Mr. SUNUNU. Until yesterday.

Ms. GAFFNEY. Right. Well, very recently.

Mr. SUNUNU. Or was the initiative that began just yesterday, was that directed toward customers or was that directed through the bureaucracy? In other words, is that an attempt to set in place a verification system or simply to double-check with customers?

Ms. GAFFNEY. No, it is intended to be a verification system, and this is a system that—it matches—

Mr. SUNUNU. Who did the letters go to?

Ms. GAFFNEY. Residents in D.C.

Mr. SUNUNU. Right. So how is sending a resident a letter saying tell us again what your income is any different than just asking them verbally upon application and not actually verifying?

Ms. GAFFNEY. What this letter does is it says we have matched what you told your housing authority your income was against IRS and Social Security data, and we find that, based on that match, you underreported your income by \$10,000. You must now—

Mr. SUNUNU. OK. So this is a case where—I am sorry. So they have actually done the verification through the IRS.

Ms. GAFFNEY. Right. Right. You must now march yourself to the housing authority and give them this information.

Mr. SUNUNU. Is there any proposal to expand that beyond the D.C. area?

Ms. GAFFNEY. Oh, yes. The mailing of the letters to the residents was to have begun in March. All of a sudden it has just been moved up.

Mr. SUNUNU. Moved up.

Ms. GAFFNEY. They have two hundred—

Mr. SUNUNU. Well, you know we are on an accelerated appropriations cycle this year.

Ms. GAFFNEY. Yes. There are 280,000 letters that are going out nationwide.

Mr. SUNUNU. Thank you very much. Thank you.

Chairman KASICH. Well, I want to thank all of you for being here, and what we hope to do is, again, create these task forces and have members chair them, and I think what you are going to end up finding is that we are going to call each of you back, along with the GAO, to focus on some of these things.

The first thing I am going to tell you is we have got to find a way in which people can do their own books. I just think that ought to be the one principle. We ought to know where the money is. We ought to know where it goes. We ought to know what it goes for. But we just have to break this down somehow, and I think I have got to figure out a way to institutionalize this in this committee now.

Our highest year was 1997 where we wrote the budget, basically, big chunks of it, and now we are into surpluses, and our role is different now, particularly with surpluses, nobody is really too interested in saving money. But they are interested in reform.

So we are going to figure out a way to do this, and I would like to be able to accomplish some things this year. Hey, if we just got it done, that we got the IRS and the Education Department to work together on a match and actually accomplished it, that would be significant.

Yes, ma'am?

Ms. LEWIS. If I could just add one thing, I would like to note that for the brand-new FAFSA, the Free Application for Federal Student Aid, for the year 2000–01, the Department, with OMB's approval, did change that form to note that the Secretary of Education has the authority to verify income reported on this application with the Internal Revenue Service. So the actual law that was passed was incorporated into the form, which is up on the Web, and obviously it is in hard copy. So it does perhaps—

Chairman KASICH. Well, like Andy Griffith—

Ms. LEWIS [continuing]. Act as a deterrent to someone who may be thinking—

Chairman KASICH. Right.

Ms. LEWIS. The only other thing, if I may add—

Chairman KASICH. Well, let me just—what you are saying is like Andy Griffith told the guy, “Put the signs up saying we have radar.” The guy says, “We don’t have any radar.” He says, “Yeah, but if you put the sign up, they might think we have the radar.”

I mean, I guess that is what that is. You know, like, well, we could check. But you are not checking. Let’s not talk—I mean, we have got—

Ms. LEWIS. It is not a verification. It is simply a notice—or the persons who put the security sign in front of their house and don’t actually have the contract.

Chairman KASICH. Right.

Ms. LEWIS. But it was intended to be put in there to bring this to persons’ attention. The only thing, if I may add, perhaps out of scope here, is I am very privileged to testify with my brand-new colleagues here in the IG community before this committee. I have known Susan Gaffney as a professional, a career civil servant back at OMB, as an inspector general. She is a person of integrity, very committed to her job, and the job she does at HUD. And I recognize Mr. Markey is not here. He had to leave.

Ms. GAFFNEY. Please stop this.

Ms. LEWIS. But it is very important for me to put that on the record.

Chairman KASICH. I think she did all right there. [Laughter.]

I will say to you, Ms. Lewis—it is clear why Ed left. No, I am just kidding.

Listen, I would want to say to you that, my mother used to teach me lessons about the people that would stick up for you. And it’s true in our society today there just aren’t enough people sticking up for enough people. And that is very nice of you. I am just telling you as another person. For you to say that about Ms. Gaffney is awfully nice, and that says a lot to me about you.

So I think she is going to do just fine, and I think she gives as good as she gets, from what I understand, of this ongoing soap opera. [Laughter.]

But somehow we need to recognize the fact that the people at HUD are making an effort. Some of these efforts, a lot, are coming into play, just recently, but they are making an effort there. And at the same time, we have a long way to go. These systems are enormous. And we are just going to keep at it, and we are not—nobody here is intending, to bang on anybody or cast aspersions on anybody. Just so we are all plugging together and working together, and I think that is what all of you want. It is certainly what I want.

But I want people to know that this isn’t the end of this. I mean, I hope not. I don’t want to be another politician to say I shall not and then I do. But I would ideally like to keep this going.

I have to tell you honestly that these efforts can only happen if I can get my colleagues to be interested. And if we had not been out of session, more members would have been here. My personal view is that since everybody can get a piece of this in this Budget

Committee and carry and make something theirs, that is what gives us the greatest opportunity to be able to really carry this on and get some good things done. And then wouldn't it be a wonderful thing if you could give us things and we could actually do something. I mean, that would make things really great. And that is where I hope we are going to go with this. We just have to wait and see.

I have to tell you that we cannot do these things without GAO and the IGs. I don't know how—I would like to have my own staff to do investigations independent from all of you, but I don't have that and I can't do it. So we need you, and we are going to put our staff into this as well, and we want to be as constructive as we can.

But I appreciate all of you being here. I appreciate all of your hard work. I also want to tell you that I also appreciate how it is sometimes when you are uncomfortable in the process of doing your work. You have to go in those buildings, and when you show up, it is kind of like somebody calling into the boss and saying, "Mike Wallace just showed up from '60 Minutes.' Isn't this exciting?" You know, and you have to keep going back in there, and it is not an easy job. You have a tough job. But you have to do it.

When you get to the point where you can't do it anymore, then you have got to let somebody else do it.

But thank you all very much, and I look forward to further contact.

Mr. HOEKSTRA. Mr. Chairman.

Chairman KASICH. The gentleman from Michigan.

Mr. HOEKSTRA. I ask unanimous consent that all written statements and any written responses to questions may be included in the record.

Chairman KASICH. Does anybody object to that? Ms. Gaffney, do you want to object to that? [Laughter.]

OK.

[The prepared statement of Congressman Paul Ryan follows:]

PREPARED STATEMENT OF HON. PAUL RYAN, A REPRESENTATIVE IN CONGRESS FROM
THE STATE OF WISCONSIN

Thank you, Mr. Chairman, and thank you for giving us the opportunity to explore possible fraud, waste and abuse in the Federal Government. I believe this issue, unfortunately, is in danger of being completely overlooked and ignored in the current era of budget surpluses.

I think that we would all agree here that if any government fraud, waste or abuse exists, it should be addressed and eliminated regardless of what the current budget circumstances are. There is a temptation, as seen in the President's budget proposal, to spend the surplus and automatically increase spending each year without giving any thought for the need to aggressively examine whether the Federal Government could be made into a more efficient machine. This is very troubling to me.

The constituents in the District I serve provided me with troubling examples of waste in the Federal Government. I turned to them for their recommendations from their own personal experience and observations.

Gregory Campbell, the President of Carthage College, brought to my attention a perfect example of waste in the Federal Government. The Immigration and Naturalization Service (INS) requires colleges and universities to collect a \$95 fee from each foreign student and remit it to the INS. To assist colleges in implementing this requirement, the INS is developing an internet-based reporting system (The Coordinated Interagency Partnership Regulating International Students or CIPRIS). CIPRIS, however, is behind schedule. Nonetheless, the INS regulation stipulates that fee collection is to be retroactive to August 1, 1999. This means that institutions like Carthage College will be required to submit college fees for several years before the system is operational. Even worse, because the INS is behind schedule

to meet their own legislative requirement, this regulation poses an unfunded mandate on these educational institutions.

Another recommendation came from Steven C. Molnar, Lieutenant of Police in Franksville, Wisconsin. Lt. Molnar told me that Congress should look more closely at the Community Oriented Policing (COPs) Program to make sure that it is truly contributing to the reduction in crime. And he's right. He is concerned that in the end, COPs may not achieve the original goals and objectives it was set out to do.

Finally, the overwhelming response from my constituents is that taxpayers are victimized by wasteful government regulations in two ways: (1) they have to spend a great deal of time and money to comply with wasteful, excessive regulations and (2) they have to fund these regulations and implementations with their hard-earned tax dollars. Gary Huss, President of Hudapack Metal Treating in Elkhorn, Wisconsin put it best when he said, "In many cases, a solution is proposed, mandated, and backed punitively before the problem is defined. Expensive solutions searching for a problem."

Mr. Chairman, there is no excuse to put taxpayers in the position of paying for and being victims of government fraud, waste and abuse. Holding government agencies accountable in the era of budget surpluses is just as important as when the government is operating under a budget deficit. I appreciate the opportunity to work with you and my colleagues on the committee to make this a priority and look forward to implementing these priorities in the upcoming budget.

Thank you.

Chairman KASICH. We will stand adjourned.
[Whereupon, at 2:42 p.m., the committee was adjourned.]

