January 23, 1990

The Honorable John Glenn
Chairman, Committee on Governmental Affairs
United States Senate

The Honorable John Conyers, Jr.
Chairman, Committee on Government Operations
House of Representatives

This letter responds to your requests expressing your concern about the magnitude and type of problems at the Department of Housing and Urban Development (HUD) and whether those problems, with their corresponding costs to the taxpayer, could exist at other departments and agencies. I have been concerned about the possibility of other HUD-type problems for some time and, unfortunately, I am convinced that they do indeed exist. GAO has been developing a program to help deal with this matter which may address your concerns.

As you know, we completed our review of the agencies' reporting under the Financial Integrity Act (FIA) and issued our report on November 29, 1989. We concluded that since passage of the act 7 years ago, it is evident that the government continues to be plagued by serious breakdowns in its internal control and financial management systems. Unless something more is done to correct the material deficiencies in management information and accounting systems, and material weaknesses in internal controls, major losses of federal funds and the collateral fraud and abuse incidents will continue.

The basic deficiencies are known and, in many instances, have been known for many years, but they remain uncorrected. It is not enough for agencies to identify problems; they must act effectively to correct them. Currently, no mechanism exists to ensure that agencies take corrective action.
Because of my concern about the potential for other HUDs or programs with significant weaknesses, we are developing plans to undertake a special audit effort. This effort will help ensure that areas likely to result in material losses have been identified and that appropriate corrective actions are being taken to stem or minimize the losses. In our discussions with your staff and in our testimony on November 29, we indicated that we were in the process of compiling a list of areas we intend to target. We have now completed our initial list, which I have enclosed.

The administration is also aware that such problems exist in the federal government, as was stated by the Director of the Office of Management and Budget (OMB) in his testimony before the Senate Committee on Governmental Affairs. "The recently exposed HUD problems are not unique, not merely peculiar to a particular agency under what some describe as absentee management.... There are analogous problems in other agencies." In October 1989, OMB issued to each agency its critique of agency reporting under the Federal Managers' Financial Integrity Act (FMFIA), a list of areas they have considered to be "high risk," and a list of key elements necessary to achieve early identification and correction of problems.

OMB's list of "high risk areas" initially encompassed 16 agencies having 74 areas of vulnerability. OMB subsequently issued an additional list of 14 of the smaller agencies having 28 areas of vulnerability. We will, of course, be alert to vulnerable areas in all of our work. Recognizing our resource limitations, we have selected our initial list based on our knowledge of the problem areas from our previous work, and other criteria, including the magnitude of the problem, the likelihood of achieving savings, and what additional work may be required.

The active involvement of the Congress is critical to achieving corrective action. Your committees have demonstrated a strong interest in improving internal controls and financial management systems throughout the government and have exercised important leadership roles for many years. I anticipate that your interest will continue and that each of you will support our program and the steps we recommended in the FIA report.

I appreciate your interest in this subject, and I hope to meet with each of you to review our initial list of
vulnerable areas and discuss our approach to this issue. I look forward to working closely with your committees and other interested committees in the Congress as we move forward in this important area.

Sincerely yours,

Charles A. Bowsher
Comptroller General
of the United States

Enclosure
INITIAL AREAS SELECTED
FOR SPECIAL GAO AUDIT OR REVIEW

Resolution Trust Corporation - The management and disposal of approximately $200 to $300 billion of thrift assets will pose unprecedented management problems. A sale of this magnitude is unparalleled in history. The desire and potential to acquire these assets at bargain basement prices will make this area highly susceptible to fraud, waste, and abuse.

Internal Revenue Service Receivables - The existence of accounts receivable in excess of $60 billion which have grown about 300 percent since 1980 places this issue in the significant potential loss area. In light of the budget deficit, the potential for reducing or stabilizing the growth rate offers major dollar savings and thus warrants special review and oversight.

Management of Seized and Forfeited Assets - This issue has been characterized by mismanagement which has been the subject of considerable press attention. Responsibility for managing the program rests with the Customs Service and the U.S. Marshall's Service. Both organizations have been identified by their respective departments as having significant internal control weaknesses. Improvements in the management and control of this program will lend support to the war on drugs and increase public and congressional confidence in the program.

Medicare Questionable Claims - The tens of billions of program dollars coupled with considerable potential for fraud and abuse indicates a high potential for financial savings from our efforts. Identified payments of $527 million by Medicare in 1985 that should have been paid by private insurance carriers illustrate the magnitude of potential savings.

ERISA/PBGC - The Department of Labor's and IRS's enforcement of ERISA has a significant impact on ensuring that employee benefit plans are free of mismanagement, fraud and abuse that place plan assets at risk and threaten the benefits of plan participants. The adequacy of their oversight has a direct financial effect on the potential for loss by the Pension Benefit Guaranty Corporation, an organization that has been unauditible in the past. The underfunding of approximately 20 percent of the plans insured by PBGC is estimated at $20 to $30 billion but is concentrated in particular industries where downturns could have a significant impact. The potential $2.2 billion
impact on the fund of one company's bankruptcy, LTV Corporation, demonstrates the vulnerability of this program, and thus the taxpayers' exposure to potential losses.

**Guaranteed Student Loans** - The large number of banks, state agencies, and schools participating in guaranteed student loan programs coupled with poor systems to protect the federal government's financial interest creates the potential for significant abuses and losses. A high proportion of defaults and publicized abuse by certain proprietary schools suggest the need for improved program controls.

**State Department Real Property Management Overseas** - There is adequate evidence of waste, mismanagement, and poor controls in this area as illustrated by the construction fiasco at the U.S. Embassy in Moscow. There is high potential for financial savings through better property management. Corrective action over the years has been minimal, but recently State has begun to show an interest in addressing these issues.

**DOD Inventory Management Systems** - Department of Defense inventories exceed $100 billion of which unneeded or excess inventory exceeds $30 billion. The excess inventory along with numerous other indicators (e.g., the failure to cancel orders where excess stock is already on hand) reflect financial management problems. Management incentives focus on filling orders and obligating funds. There is no corresponding focus on reducing costs or controlling or securing stock, i.e., economy and efficiency. The current pressure to reduce the DOD budget in response to recent world events provides additional incentives to make major improvements in the supply system.

**DOD Major Systems Acquisition** - The total estimated cost of major systems currently being developed or produced exceeds $900 billion. Following established management controls to deliver capable and supportable weapons to the user when and where needed, and at reasonable cost, has been the exception rather than the rule. As a result, DOD continually buys higher cost systems which substantially exceed original estimates, are delivered much later than originally scheduled, and do not meet the capabilities advertised. GAO will review the effectiveness of management initiatives to address these long-term problems and their means of achieving savings.
NASA Contract Management - NASA will spend $11 billion in 1990 on contracts and has a very decentralized contract administration process. In this environment, there is considerable potential for mismanagement, fraud, and abuse. The potential for large savings exists if better contract controls and oversight can be achieved.

Farmers Home Administration Loan Programs - FmHA has made billions of dollars of credit available to the nation's farmers. Delinquent farm loan borrowers held $11.1 billion, or 48 percent, of the agency's $23.3 billion in outstanding loans as of September 30, 1989. FmHA is responsible for protecting the government's interest, as well as helping farmers who cannot get help elsewhere. Recognizing congressional concern to reduce the deficit, any potential for controlling loan losses warrants added review and oversight.

Superfund Enforcement and Contractor Oversight - The Congress has authorized $10 billion for the Superfund program but estimates of federal funds needed to complete the cleanups are many times that amount. To avoid wasting federal resources, the Environmental Protection Agency (EPA) needs to (1) ensure that parties who contaminate sites pay their fair share of the clean-up costs and (2) effectively manage clean-up contractors who get over 75 percent of Superfund's outlays. GAO will explore cost and conflict of interest control and whether EPA uses its full authority to compel private party cleanup.

Urban Mass Transportation Administration Grants - UMTA currently manages active grants totaling $30 billion with over $3 billion in new grants each year. The number of staff available to UMTA for project oversight is limited. Based on recent GAO survey work, increased oversight of the grant application review process and adherence to grant provisions is needed. The criteria for deciding what projects get funded and in what amounts is limited, and, in some cases, projects are funded at the sole discretion of the Administrator.

Department of Energy Contractor Oversight - DOE relies on contractors and consultants for most of the work needed to fulfill its mission. For example, DOE obligated about $15 billion for procurement in 1988. The Department has had a history of inadequate contractor oversight and bonus awards to contractors in situations that would appear to be highly questionable. While this may be due in part to lack
of expertise or inadequate staffing, it also may be due to DOE's philosophy of "least interference" with its operating contractors. GAO will examine DOE's potential for improvements in control, accountability, and efficiency.