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MANAGEMENT OPERATIONS STAFF

PREFACE

This is the fifth semiannual report of the U.S. Department of Agriculture's Office of Inspector General, submitted pursuant to the requirements of the Inspector General Act of 1978. The report covers the period from October 1, 1980 through March 31, 1981. During the reporting period, we issued 874 investigative reports and 243 audit reports. Our audit and investigative work during the period identified, or resulted in, approximately \$90 million in recoveries, savings, erroneous payments, management improvements, incorrect loan amounts, penalties, claims, fines and judgements. Our investigative work resulted in 381 indictments and 235 convictions during the period. We have continued to target our audit and investigative resources on those programs which we believe have the potential for wasting the largest amount of money and those which pose substantial risk to employee integrity. For example, the program which received the most audit and investigative attention during the period was the Food Stamp Program. Most of our indictments were for felony offenses such as food stamp trafficking, and fraud in relationship to departmental loan programs. While this report does not describe in detail all of the problems and recommended corrective actions contained in our audits and investigations, it does describe those which we believe to be the most significant.

RESOURCES

The lack of sufficient resources, both travel and personnel, continued to be a major impediment in terms of operating at the effectiveness and level which was envisioned by our 1981 budget. While our approved personnel ceiling for 1981 was 931 persons, the recent freeze has lowered the figure to an actual on-board strength as of March 30, 1981 of 890 people. Our effectiveness has also been hampered by restrictions on travel. While the overall objective of saving money through travel restrictions and a personnel freeze is worthy and one we subscribe to, travel and personnel are essential for us to conduct audits and investigations. The programs of the Department are widely dispersed geographically, and our auditors and investigators must travel in order to be effective in their jobs.

OMB Circular A-102, the single audit concept, has continued to require significant resources for its implementation. During the reporting period we have worked with OMB and other Inspectors General to develop uniform policies and procedures for implementation of the Circular. In order to assist us in developing appropriate departmental A-102 policies and procedures, we have also conducted a survey of a number of non-federal audits of selected USDA programs. We are now conducting seminars to explain the requirements of Attachment P of the Circular to USDA personnel, recipients and other interested persons. We have also devoted considerable resources to OMB Circular A-76 (Policies for Acquiring Commercial or Industrial Products and Services Needed by the Government). These Circulars plus other added

responsibilities have had a significant effect on the use of OIG resources and indeed have caused us to divert personnel from our audit and investigative operational activities. These additional responsibilities coupled with a decrease in both travel and personnel considerably diminish the amount of audit and investigative coverage we can devote to the major programs in the Department.

IMPLEMENTATION OF RECOMMENDATIONS

During the reporting period there was a major change in the administration of the Department's programs. We are pleased to note that we have received excellent cooperation from Secretary Block, Deputy Secretary Lyng and the Under and Assistant Secretaries and Program Administrators who have the responsibilities for the programs which we are auditing. Specifically, we are optimistic since the significant and endemic problems we have catalogued in this and other reports relating to the domestic food assistance programs and the rural development programs of the Farmers Home Administration are receiving serious and aggressive action by the appropriate officials.

Robert E. Magee
Acting Inspector General

TABLE OF CONTENTS

	<u>Page</u>
PREFACE	i
SECTION I - SIGNIFICANT PROBLEMS, ABUSES OR DEFICIENCIES AND RECOMMENDATIONS FOR CORRECTIVE ACTION	1
DOMESTIC FOOD ASSISTANCE PROGRAMS	1
Food Stamp Program	1
School Feeding Programs	20
Child Care Food Program	25
Summer Food Service Program for Children	31
Special Milk Program	35
Commodity Distribution Program	36
RURAL DEVELOPMENT PROGRAMS OF THE FARMERS HOME ADMINISTRATION	42
Business and Industrial Loan Program	44
Community Programs	60
Evaluation of Loan Security and Repayment Ability	65
DEPARTMENTAL ADMINISTRATION	71
USDA Travel Management	71
Consultant Services	72
Year-End Spending	74
Department Management	78
Cash Management	79
Internal Controls	80
Systems Monitoring	82
Property Management	85
INTERNATIONAL AND COMMODITY OPERATIONS	88
SECTION II - SUMMARY OF INVESTIGATIVE AND AUDIT ACTIVITIES	92
INVESTIGATIONS	92
AUDITS	105
SECTION III - MONEY OWED TO THE DEPARTMENT OF AGRICULTURE	118
SECTION IV - EMPLOYEE COMPLAINTS (HOTLINE)	119
APPENDIX - Listing of Audits	

SECTION I
SIGNIFICANT PROBLEMS, ABUSES OR DEFICIENCIES
AND RECOMMENDATIONS FOR CORRECTIVE ACTION

DOMESTIC FOOD ASSISTANCE PROGRAMS

The food assistance programs administered by the Food and Nutrition Service (FNS) obligated \$13.5 billion in FY 1980. These programs are budgeted for \$15.5 billion (including a \$1.2 billion supplemental appropriation) for FY 1981, or 56 percent of the USDA budget, and \$13.9 billion in FY 1982, or 50 percent of the Department's proposed budget. Because of the large sums spent for these programs and their high vulnerability to fraud, abuse and waste, OIG expends significant audit and investigative resources on them.

FOOD STAMP PROGRAM

Expenditures for the Food Stamp Program in 1980 amounted to \$9.15 billion. FNS estimates the FY 1981 expenditures at about \$10.9 billion and those of FY 1982 at about \$9.8 billion, assuming passage of all proposed legislation. The general purposes of the program have remained the same for the past twenty years. Then, as now, the program is designed to improve the diet of the poor, increase the consumption of food, use up excess food production, and provide general assistance to those poor not aided by any other government program. For the past several years we have conducted numerous audits and investigations of the program. Indeed, the program receives more OIG attention than any other single program in the Department. During this reporting period we have continued our intensive audit and investigative coverage.

The following is a description of some of the operations of the Food Stamp Program and our recommendations, based on audit and investigative findings, to reduce fraud, abuse and waste further.

CERTIFICATION AND VERIFICATION

The basic factors determining food stamp eligibility and benefit level are income, family size and, secondarily, liquid assets. Income for the Food Stamp Program means that amount a household has at its disposal to purchase food after necessary expenses are deducted. Thus, regulations stipulate a number of standardized deductions which, if applicable, can be subtracted from gross income to determine net income. Regulations also require that the certification worker verify an applicant's income and expenses. The amount of food stamps received by a household is based upon its net income and family size.

Quality Control

The largest dollar drain in the Food Stamp Program occurs because of certification errors, for instance, incorrect information provided by applicants and miscalculations. The most recent data on certification errors, from the period October 1, 1979 through March 3, 1980, show that 10.2 percent of food stamp dollars, or approximately \$807 million on an annual basis, are overissued due to errors in the certification process. Since underpayments constitute another 2.4 percent of the dollars, the net loss to the Federal government is 7.8 percent, or approximately \$616 million. About 50 percent of the mistakes identified are client related.

These data come from food stamp quality control reviews conducted by all the States. The reviews measure the correctness of eligibility and benefit level determinations for food stamp cases within a specified six month period.

Samples of households are statistically selected from both households currently participating in the Food Stamp Program and those either previously participating or denied program benefits. For each case in the sample, independent reviews are conducted of all information relating to eligibility and correct coupon allotment. These data are compared to those from the previous certification. When information varies, the source of the error is found and the incidence and dollar amounts of any errors are tabulated. The 1980 Amendments to the Food Stamp Act provide for an adjustment from 50 percent up to a maximum of 65 percent of the Federal share of administrative expenses, depending upon the error rate or reduction in error rate of the State, to provide incentives to the States to reduce certification errors. A similar sanction system penalizes the State with high error rates.

We are presently conducting an audit of the quality control system. Our auditors are verifying State sampling procedures and, for a subsample, independently evaluating the certification and benefit levels. The audit will provide a nationwide certification error rate, evaluate State agency compliance with the prescribed quality control system, determine what uses

can be made of the quality control results, estimate the administrative costs and provide an independent evaluation of the design and implementation of the system.

Verification Procedures

We have consistently recommended better verification of information provided by the applicant which affects eligibility and benefit level. In an audit we conducted of selected local food stamp projects in several Southeastern States, we found that various percentages of those recipients who reported earning income had underreported their income. These percentages ranged from 10 to 40 percent. Subsequent audits have disclosed significant underreporting in other States. We believe the underreporting of income to be the most serious violation of the integrity of the Food Stamp Program.

New regulations, issued on January 13, 1981, require certification workers to verify gross income, alien status, utility expenses if in excess of the standardized allowance, medical expenses, social security numbers, residency and the identity of the applicant. The State may also verify such factors as liquid resources and household size. Household composition and citizenship can be verified but only if questionable. These regulations differ from previous regulations in requiring verification of residency and identity, and in allowing States to require verification of most other factors relating to eligibility and benefit levels. However, they reiterate the requirement that documentary evidence is the primary source of verification for all items

except residency and household size. Documentary evidence is defined as written confirmation of a household's circumstances. Other methods of verification are restricted. For instance, the names of third parties who can confirm the applicant's information, such as an employer, are furnished by the applicant. Home visits may only be made if the documentary evidence is deemed insufficient and must be scheduled in advance with the applicant. Given these restrictions and the high incidence of underreported income found by our audits, we believe one way to prevent recipient fraud is to require more stringent documentation. Documentary evidence should consist primarily of printed forms, such as W-2 forms, pay stubs, and birth certificates.

Matching

Another way to decrease certification errors is to use computer matching of recipient reported eligibility data with similar data maintained by other Federal and State agencies. We believe such matching offers great potential for detecting fraud and error in the Food Stamp Program, particularly for reported income. Substantial program savings could be realized if this technique was utilized more frequently and particularly "up front" or at the time of the initial certification.

With the passage of the 1977 Food Stamp Act and 1979 and 1980 amendments to the Act, the Congress has also recognized the benefits of computer matching. The 1979 amendments allow the Secretary of Agriculture to require as a condition for participation in the program that each household member furnish

their social security number to the State agency. The State agency is also permitted to use the social security number in determining the accuracy and reliability of information given by households and in preventing duplicate participation.

The 1980 amendments to the Act further increase the authority of the Secretary and State agencies to utilize matching techniques. These amendments allow the Commissioner of Social Security to disclose information from income tax returns with respect to net earnings from self employment, wages, and payment of retirement income. The 1980 amendments also encourage States to improve their computer processing capabilities by allowing the Secretary to pay 75 percent of the costs incurred by a State in the planning, design, development or installation of automatic data processing and information retrieval systems that would assist the State in meeting the requirements of the Food Stamp Act.

Congressional support for computer matching is best summarized in a report by the Committee on Agriculture of the House of Representatives. The report stated that the computer matching legislation would enable the Department and the States to verify all income information in a manner that cannot be manipulated in any way by the applicant or recipient. The Committee further explained that computer matching is the "single most effective technique now in existence for avoiding error and fraud and preventing benefit payments to ineligible persons and benefit overissuances to eligible ones."

In spite of this strong Congressional support for the use of computer matching techniques, few States have actually utilized such techniques in their Food Stamp Program administration. Since 1979 States have been allowed to match against two of the data files of the Social Security Administration, the State Data Exchange (SDX) and Beneficiary and Earnings Data Exchange System (BENDEX). FNS is currently drafting regulations to give States the authority to match against unemployment compensation records and Social Security Administration wage files.

OIG Matching Efforts

We have utilized computer matching techniques during our Food Stamp Program audits and investigations for a number of years to determine the value of matching, to specify the amount of underreporting of income and, on a sample basis, to project the extent of problems in the certification process in a cost-effective way. We are presently working with States to demonstrate the effectiveness of computer matching and ways to incorporate it into individual State systems. The following are some examples of our more recent efforts.

Dade County, Florida

In our recently completed audit in Dade County (Miami), we matched the income of a sample of 350 households participating in the Food Stamp Program in September 1979 with the State Employment Security Bureau income records. Projecting our findings to the approximately 86,000 participating households,

we found that 32,000, or about 37 percent, had some type of error. We estimated that the total dollar loss to the program was about \$1 million for this one-month period.

Of the errors causing program losses, 70 percent were due to underreporting income. Our estimate of the dollar loss attributable to income underreporting was \$813,000 of the total \$1 million.

Florida is now in the process of refining their computer system. Program officials project that by August 1981, they will have the capability in Miami to compare income reported by the applicant at the time of certification to the income reported to the State Economic Security Bureau. This will enable State officials to detect applicants underreporting of income before benefits are issued. It should also act as a deterrent to recipient underreporting.

Memphis and Nashville, Tennessee

We have recently completed our audit fieldwork on food stamp operations in Memphis and Nashville, Tennessee. At both locations, we matched income reported on the food stamp application with that reported to the State Employment Security Bureau. In March 1980, there were approximately 59,000 households in Memphis and 22,000 households in Nashville participating in the Food Stamp Program. We found that 1,601 households had failed to furnish complete or accurate income data to the food stamp offices. While we have not completed an exact determination of the dollar value of the loss to the

government, our current estimate is that it amounts to approximately \$2.5 million for the various periods these households underreported their incomes.

In addition to the affect on the Food Stamp Program of underreporting income, we also reviewed its impact on programs of the Department of Health and Human Services, such as Aid to Families with Dependent Children (AFDC), Supplemental Security Income (SSI), and Medicaid; and the housing assistance programs of the Department of Housing and Urban Development (HUD).

Of the 1,601 identified problem food stamp cases, about 667 of these households participated in AFDC, 735 in Medicaid programs, 95 in SSI, and about 144 were receiving HUD housing assistance. The estimated dollar value of improper benefits for AFDC alone amounts to approximately \$750,000. Investigations or claims determinations are proceeding or planned in each of these cases.

The U.S. Attorney has agreed to prosecute approximately 100 cases, preferably those involving more than one Federal program. After State and local investigators complete their work, other cases will be adjudicated in the State courts or through administrative fraud hearings.

Atlanta, Georgia Metropolitan Area

When food stamp projects are administered county-wide and when metropolitan areas spill over into other States, the possibility exists that recipients can illegally apply for and receive program benefits in more than one food

stamp project jurisdiction. We have just recently completed audit work in metropolitan Atlanta, which is comprised of DeKalb and Fulton Counties. These two counties administer the Food Stamp Program independently of each other. Thus, without proper controls or periodic matching between the two counties, simultaneous participation by an individual in both counties would not be detected. Such a control did not exist at the time our audit was completed.

Our audit showed that 48 persons in 24 households participated in the Food Stamp Program in DeKalb County while simultaneously participating in Fulton County. While the 48 persons represented a small portion of the 46,000 households (130,000-140,000 persons) participating in the two counties at the time of our audit, these cases are obvious fraud cases. They are easily detectable through a simple, low cost matching procedure.

Legislative Recommendations

In our September 30, 1979 semiannual report to Congress, we recommended that Congress consider requiring rather than just permitting computer matching of available wage data with recipient information. We also strongly endorsed the computer matching provision introduced by the Department and contained in the 1980 amendments to the Food Stamp Act in our semiannual report, although this legislation only permitted computer matching rather than making it a requirement.

Because of the benefits computer matching offers as described above and because of the relatively few States utilizing such techniques, we again suggest that Congress consider requiring computer matching, as it has previously done for AFDC, in those States with the capacity to do it; and, strongly encourage States without the capability to obtain it.

ISSUANCE SYSTEMS

In general, recipients receive their food stamps through one of three types of issuance systems. One type, direct mail, involves mailing the food stamps directly to all recipients, for instance, rural residents, or to certain classes of recipients, such as the elderly and disabled. Although convenient for the recipient, this system is vulnerable to recipient fraud since there is no evidence that they received or did not receive their original issuance. It is also tempting to criminals who specialize in stealing mail.

During 1980, we evaluated direct mail issuance procedures to determine whether mail losses of food coupons were increasing and whether the Food and Nutrition Service regional offices and State agencies were effectively monitoring mail issuance systems. Our audit was performed in Alabama, California, Florida, Illinois, Tennessee, West Virginia, Wisconsin, and Utah.

Statistical data gathered during the audit period from the eight States disclosed that food coupons mailed directly to recipients amounted to about \$33 million. Replacements of food coupons for the same period amounted to

about \$337,000, or a little more than one percent. Although the number of replacement issuances in the direct mail systems was small, the potential for loss remains large, and continued monitoring of these systems will be necessary.

Specifically we are concerned that areas which are not rural are beginning to use direct mail issuance. This system is attractive to State agencies because of the low cost of administration. Presently, the Federal government is liable for the value of replacements resulting from mail losses. We believe FNS should establish a loss tolerance rate to limit the amount of Federal liability. The State agencies would have to absorb the cost of losses beyond the tolerance rate or switch to a more cost-effective system.

In the household issuance record system, recipients receive their food stamps when they present themselves at the food stamp office. The signatures of recipients are checked with those on file before the coupons are issued. While this system is particularly vulnerable to theft by food stamp employees if two or more plot collusion, it is still the least vulnerable of the three systems. However, it is also the least common and operates primarily in small food stamp projects.

By far the most common form of issuance, and also very vulnerable, is the Authorization to Purchase (ATP) card system. Under this system a computer-generated authorization card, serially numbered with the recipient's name, address, and allotment, is mailed to the household each month. Recipients take the ATP's to coupon issuers who issue the food stamps after

checking recipients' food stamp identification cards. This system contains the weaknesses of both other systems. It is vulnerable to recipient fraud if recipients falsely claim they did not receive their cards. The authorization cards are vulnerable to theft by issuance office employees, postal workers and others. In many metropolitan areas, the incidence of reported losses of authorization cards has been very high. For instance, a year ago, we pointed out that in New York City about 25,000 replacement Authorization to Participate cards were being issued each month because recipients reported that their cards were lost or stolen. About 70 percent of the reported lost or stolen cards were being redeemed, representing an estimated \$7.2 million loss to the program for the first 6 months of 1980. In October 1979, Philadelphia County, Pennsylvania, had 2,800 cases where both the original and replacement authorization cards were redeemed, resulting in program losses of \$210,000 according to our last audit. Since these audits, several demonstration projects have been developed to test methods to reduce these abuses.

New York City

In New York City, the main cause of the problem appears to be recipient fraud. In August 1980, the City began requiring recipients to pick up replacement authorizations directly from five designated locations throughout the City or from welfare centers if the person also receives public assistance. In addition, in October 1980, the City began implementation of a

Rapid Access Reconciliation System. Under this system the recipient is required to wait five working days following a request before receiving a replacement card. This five day delay, combined with a shortened eight day life for the authorization card, maximizes the number of original authorization cards which can be cleared by the new reconciliation system. If the original is redeemed and reconciled during the interval, the recipient is sent to a central location where the signature on the request for the replacement card, completed five days previously, is compared to that on the original redeemed card. Only if they do not match is the recipient given the month's food stamps. The procedure of sending the recipient to the central unit by itself has eliminated some of the problem. The number of replacements has dropped sharply and the possibly fraudulent duplicate issuances have been sharply curtailed.

Pennsylvania

In September 1980, Pennsylvania began a demonstration project in three districts in Philadelphia and one in Pittsburgh that should eliminate the problem in those districts. The project involves a direct delivery system in which certain recipients are not mailed their authorization cards. Instead they go to a specific issuance agent to sign their authorization card and, at the same time, pick up their coupons after presenting photo identification cards. This eliminates the possibility of mail theft or of recipients fraudulently claiming the nonreceipt of their authorization card.

From September 1 through December 31, 1980, only 20 authorization cards were replaced in the areas in which this direct delivery system was being tested. These replacements were necessitated because of clerical problems. The Food and Nutrition Service estimates savings of \$22,000 a month from this system. However, in other areas of the same cities, multiple redemptions have been continuing at a high rate. The Food and Nutrition Service has just given the State permission to expand direct delivery into the rest of Philadelphia and Pittsburgh. They are also modifying the system to allow only a 5 day life to an authorization card to minimize the dangers of theft at the issuance centers.

A variation of this system is being used in Florida. In that State cashiers use on-line terminals which directly access the recipient's certification file stored in a central computer. When recipients present themselves at the food stamp office to obtain their monthly allotment, they present an identification card to the cashier. The cashier uses the card to directly access the recipient's file. After the file is checked, the terminal produces an authorization document. The recipient signs this form and the coupons are issued.

As a result of our audit findings, the Food and Nutrition Service has proposed regulations to require alternate issuance systems for recipients after their second request for a replacement authorization card within a six month period. The regulation would also give State agencies a period of up to ten days to issue replacements. This provision would increase the

likelihood of detecting both fraudulent and erroneous duplicate issuances.

The Federal government is currently assuming liability for losses in the Food Stamp Program of stolen authorization cards and coupons, even after receipt. At the present time, regulations require States to replace ATP's and coupons which are reported stolen by the recipient, as long as the recipient produces a police report describing the loss. FNS is presently considering prohibiting replacements of coupons from such thefts. We support this provision.

Identification Cards

For several years we have been recommending the use of photo identification cards to determine the identity of recipients accurately when issuing benefits. A 1980 amendment to the Food Stamp Act allows the Secretary of Agriculture, in consultation with the Inspector General, to require photo identification cards for recipients. Proposed regulations were issued in January to implement this amendment. The regulations propose photo identification in all project areas with 50,000 or more participants, except where the State agency requests exemptions for project areas with few duplicate issuances or with direct mail issuance. The Department could impose a photo identification requirement in areas of less than 50,000 participants if the rate of duplicate issuance is high. Exceptions to the photo identification requirement would be made for those persons certified at some place other than a food stamp office (for the elderly and handicapped) or persons whose religion does not permit them to be photographed.

The regulations would require the coupon issuer to write the photo identification serial number on the authorization or household issuance record card being redeemed. We are in agreement with the proposed regulations on all significant points and urge that they become final as soon as possible. However, we believe the key to ensuring that only the authorized household redeems its ATP is to make the coupon issuer liable for ATP's redeemed by persons other than those authorized. The coupon issuer should be required to write the serial number of the recipient's identification card, whether it is a photo identification card or the cards now in use, on the authorization document to ensure proper verification of the person redeeming the ATP. If the number is missing or if the ATP is counterfeit, altered, or subsequently found to be stolen or cashed by someone other than the authorized recipient, the coupon issuer should be made liable for any losses to the program. The cashers of U.S. Treasury checks are so liable and few Treasury checks are stolen and then redeemed.

Wholesalers

In previous semiannual reports to Congress we have indicated our concern about the ease in which wholesalers can redeem illegally obtained food stamps. Since such losses were demonstrated by our investigations, we have urged the Food and Nutrition Service to eliminate wholesalers from the program. On November 17, 1980, proposed regulations were issued to remove most wholesalers from the Program. Those regulations have not yet been issued in final form and we urge that they be issued as soon as possible.

INVESTIGATION, PROSECUTION AND COLLECTIONS

Recipient fraud, while in aggregate the greatest dollar drain in the Food Stamp Program, consists of many individual cases of relatively low dollar value. The Department and OIG, in particular, cannot investigate or establish claims against even a small portion of these infractors since we have consistently concentrated our investigative efforts on large scale food stamp trafficking. Moreover, the States, charged with implementation of the Program, bear the primary responsibility for prosecuting violations and assessing claims against individual recipients.

The Congress has cooperated with the Department by including a number of provisions in the Food Stamp Act and its amendments to induce greater prosecution and collection action by the States. The Food Stamp Act of 1977 provided for Federal funding of 75 percent of the costs of investigative and prosecutive activities. It also gave legal authority to the States to set up administrative procedures for fraud hearings. These hearings are designed to be independent from both Federal and State court systems so that State and local program officials can make the effective decisions regarding whom to adjudicate. Even so, the administrative fraud hearing system has met with resistance. States allege that the system is cumbersome and expensive and is not cost-effective when compared to the amounts of possible recoveries. However, to provide some financial incentive, the Congress, in 1979, provided that States be allowed to keep 50 percent of their fraud recoveries.

The 1980 Amendments contain an incentive/sanction system to reward States for low error rates in their quality control reviews and to penalize them if their error rates are high compared to other States. These inducements consist of an enlarged Federal share of administrative expenses for States with low or substantially reduced error rates and a commensurate reduction of Federal administrative monies for high error rates.

The Administration Food Stamp Bill contains further provisions to prod States to more vigorous law enforcement. We support the following provisions of the bill:

- o To change the charge in an administrative fraud hearing from fraud to "the making of false or misleading statements, misrepresentation, or the concealment or withholding of facts." This change may encourage more administrative hearings since a State would no longer have to prove fraud, but only misrepresentation.
- o To extend offsetting benefits (that is, procedures for reducing benefits to make restitution) to nonfraud as well as fraud claims. Nonfraud claims result from overissuances because of recipient misunderstanding of program requirements or errors by food stamp officials.
- o To modify the quality control incentive system so that States must have low or reduced error rates on both the sample of participating households and the sample of households denied benefits or terminated from the program to qualify for increased Federal funding.

- o To require States to develop corrective action plans if their quality control error rate exceeds 5 percent.

We believe that if a few States demonstrate the advantages of vigorous investigations, prosecutions and claims, the other States will follow their example.

SCHOOL FEEDING PROGRAMS

The National School Lunch Program is by far the largest of the Child Nutrition Programs. The Department's FY 1981 budget estimated that about \$3.3 billion in cash and commodities would be required to serve lunches to over 26 million children under existing legislation. In addition, over \$300 million will be used to subsidize the service of breakfast in schools. Altogether, over 85 percent of the \$4.2 billion the Department expects to spend for child nutrition will be in the school feeding programs.

Since the early 1970's, the National School Lunch Program and the School Breakfast Program have operated on a "performance funding basis." Federal payments are based on the number of meals served to children in each of the three different income categories defined in the legislation. Meals must meet certain quantitative requirements established by the Secretary. All meals receive a basic rate of Federal support. Additional funding is provided for meals served at a reduced price of 10¢ - 20¢ to children from families with income between 125 percent and 195 percent of the income poverty guidelines prescribed by the Secretary. Children from families with

incomes below 125 percent of the guidelines receive their meals free: Federal payments cover the entire cost of the free meal up to a maximum reimbursement rate (97-1/4¢ per meal for January - June 1980). For performance funding to operate properly, meals must meet requirements, children must be correctly classified according to family income and size, meals must be accurately counted and categorized according to applicable reimbursement rates, and reimbursement claims must accurately reflect counts of paid, free and reduced price meals actually served.

In the past, OIG audits and reviews of school food service operations conducted by the Food and Nutrition Service have disclosed that: (1) free and reduced price meal applications submitted by households are frequently approved by schools even though they are incomplete or invalid on their face, and (2) meal counts used to determine the amount of Federal funds claimed are often incorrect with the error most often working to the financial advantage of the school.

During May 1980, we conducted an audit of school food service in 220 statistically selected schools across the country in an effort to assess: (1) the general dimension of inflated or incorrect meal counts, (2) improper authorizations by schools for free or reduced price meals, and (3) the degree to which incorrect information on family income and/or size is furnished by parents on free or reduced price meal applications.

Our audit disclosed that:

- o Schools had incorrectly authorized free and reduced price meals for about 7 percent of the children in our sample. About 26 percent of these children were authorized free and reduced price meals even though they had no corresponding applications on file. About 36 percent had applications on file which did not contain essential household income or size data from which proper eligibility determinations could be made. Another 30 percent had complete applications on file from which incorrect eligibility determinations were made. Projecting incorrect authorizations nationwide, we estimate that at least 5.3 percent of the free and reduced price applications were incorrectly approved in the 48 contiguous States. Our projections indicate that at least \$5.7 million were overclaimed on a nationwide basis in May 1980.

- o About 30.7 percent of the applications submitted by families for free and reduced price meals that we reviewed contained incorrect household data: approximately 94 percent of these applications resulted in children receiving a greater benefit than that to which they were entitled. Statistically projecting the incorrect applications we found to the 48 contiguous States reveals that at least 2.4 million free and reduced price meal authorizations for the 1979-80 school year were improper due to inaccurate information

supplied by the applicant. We estimated that improper authorizations resulting from inaccurate applicant information amounted to at least \$171.5 million in overclaims between September 1979 and April 1980. We feel that much of the aforementioned problem has resulted from a lack of guidance provided to parents in completing free and reduced price applications--specifically in what income to report and over what period.

- o About 6.6 percent of the lunches and 8.8 percent of the breakfasts we observed were found ineligible for reimbursement due to one or more missing meal components and, to a lesser extent, errors in counting the number of meals to be claimed. The latter represented less than one percent of the error. Projecting overclaims resulting from missing components and errors in meal counts to the 48 contiguous States reveals that at least \$468,000 were overclaimed for breakfasts and \$8.4 million for lunches in May 1980.
- o Approximately 53 percent of the schools we visited claimed an average daily number of lunches which was greater than their meal counts for the day. Statistically, the average of our observed counts should be close to the mean of the average daily meal counts of the schools for the month. However, net average daily participation rates exceeded school counts by 909 lunches for all schools visited. From this, we concluded that schools or school food authorities tended to overstate

the number of meals served and thus overstated their claims for reimbursement. Projecting the extent of these inflated meal counts to the 48 contiguous States reveals that at least \$700,000 were overclaimed for May 1980.

We therefore recommended that:

- o School food authorities be required to use standard nationwide or statewide free and reduced price application forms which require all adult members of a household to furnish their sources of income and social security numbers. FNS should seek the legislative authority to obtain social security numbers. The Department's current legislative package which was submitted to Congress for consideration requests legislative authority to obtain parent or guardian social security numbers on applicant forms.
- o State agencies or school food authorities be required to routinely verify family income on free and reduced price applications by computer matching techniques. The Department's current legislative package before Congress requests legislative authority for computer income verification.
- o FNS clarify the method to be used in determining a household's annual income and who is to be counted in determining family size.

It should be noted that the Food and Nutrition Service was very critical of both the methodology and the findings of our audit. As a result, the Committee on Education and Labor in the House of Representatives requested

the General Accounting Office to review the methodology of our audit and the substance of our findings. The General Accounting Office generally agreed with both our methodology and our findings.

CHILD CARE FOOD PROGRAM

The Child Care Food Program provides grants to States to initiate, maintain and/or expand food service programs for children in nonresidential public or private nonprofit child care centers and day care homes. Both food and food service equipment assistance payments are provided. The program is administered nationally by the Food and Nutrition Service and within States by State educational agencies or FNS regional offices. States unable or unwilling to administer the program themselves have been able to turn the responsibility over to the Department. The FY 1981 Agriculture Appropriations Act, however, precludes Federal administration of additional State programs for one year. Expenditures for the program totaled more than \$204 million in FY 1980.

We recently completed an audit of the Child Care Food Program which concentrated primarily on FY 1979 program operations. Our audit covered State agency and FNS management of the program and 175 statistically selected child care institutions in 13 States. We found that: (1) FNS had not provided sufficient guidance or supervision to administering agencies and institutions to assure effective program operations, and (2) FNS headquarters

had not performed the required management evaluations of FNS regional offices and had not, until recently, analyzed State agency management evaluations conducted by FNS regional offices.

Our audit also disclosed that:

- o Seventy-nine percent of the audited institutions had submitted questionable claims for May 1979. Net questioned reimbursements totaled more than \$323,000. Extrapolating this finding to all participating institutions in the 13 States audited would indicate that questionable overclaims for the month of May totaled more than \$1.5 million. We attributed questionable claims to errors in assembling and reporting data, computational errors and claims for ineligible meals. Forty-eight of the child care facilities audited had claimed meals and snacks for more children than were actually in attendance; 31 had claimed meals which did not contain all of the required food components. Reimbursed food claims for six unapproved and six unlicensed child care institutions were also found.

- o Thirty institutions audited had received funds for the same food service costs from the Department of Agriculture and at least one other Federal agency. Dual funding of food service costs from the Head Start and Title XX programs were most frequently found; although, dual funding of labor costs from the Community Services Administration and the Department of Labor's CETA Program were also

identified. Some of the other Federal programs, such as Headstart, permit funds to be budgeted initially for food service in order to defray food service costs which are borne before USDA reimbursement is received. These funds, however, are to be recovered and used for child care services when USDA reimbursement is received. While some or all of the excess funds we found may have been used for other purposes, it is impossible to say since none of the thirty institutions had reconciled income against expenses. Total Federal funds exceeded actual food service costs by more than \$104,000 in these 30 institutions for May 1979. Projecting this figure to all participating institutions in the 13 States audited would indicate that total Federal funds for food service probably exceeded costs by more than \$532,000 in May 1979.

- o Three of the 13 administering agencies reviewed did not conduct required audits. Follow-up procedures, moreover, were either deficient or did not exist in three States; and, Departmental funds earmarked for audits were incorrectly expended or accounted for in five.

- o An insufficient number of administrative reviews were conducted in six States, and six States that conducted reviews had inadequate or nonexistent follow-up procedures to correct deficiencies noted in reviews.

- o The tiering method of reimbursement, legislated under Public Law 95-627 and effective May 1980, could have increased program costs by \$893,000, or by more than 9 percent, had it been an available option in May 1979. The tiering system permits institutions to claim free rate reimbursements for all children in attendance if at least two-thirds of their enrollment is eligible for free or reduced price meals (tier 1). Similarly, institutions may claim reduced price reimbursements for all children if between one-third and two-thirds of their enrollment is eligible for free or reduced price meals (tier 2). If less than one-third of an institution's enrollment qualifies for free or reduced price meals, then the institution is classified as tier 3 and all claimed meals are reimbursed at the paid rate. Although the tiering method was not available at the time of our review, we were able to estimate its potential impact by assuming that each institution in our sample would choose that method of reimbursement yielding the most benefit. We assumed reduced price reimbursements to be 10 cents less than the free rate and recalculated the May 1979 claim data for institutions in our sample to determine their level of reimbursement under the tiering system. We found that 128, or 74 percent, of the institutions would have received a larger reimbursement under the tiering system. It should be noted, however, that neither the Child Care Amendments of 1978 nor

the accompanying regulations require institutions choosing to adopt the tiering system to provide any additional benefits to the children despite the additional income provided to institutions under this system. Our preliminary review also indicated that the tiering system will reduce neither legislative nor administrative requirements at the institution level and may adversely affect participation rates of children from low income families.

Among the recommendations we made to the Food and Nutrition Service are the following:

- o Instruct FNS regional offices to: (1) correct deficiencies in FNS administered States, cited in our audit, which contributed to the ineligible meals, and (2) monitor corrective action in State agency administered States.
- o Issue guidance materials to administering agencies which establish criteria under which they must recover reimbursements from institutions for meals that fail to meet pattern requirements.
- o Monitor the implementation of new Financial Management Instructions to ensure that States and institutions develop operating procedures which satisfy accounting requirements.

- o Require administering agencies to determine, as a part of the annual Child Care Food Program application process, which institutions receive non-USDA Federal funds identified for food service program use and to provide detailed instructions on how such funds should be identified on claims.
- o Seek legislative change to remove the tiering method of reimbursement to institutions from Public Law 95-627.
- o Issue guidance materials emphasizing the two year audit requirement and include specific procedures for the accountability of Child Care Food Program audit funds.
- o Monitor corrective action by State agencies to determine if audit deficiencies cited in State reports were properly resolved.
- o Monitor progress of State agencies in meeting administrative review requirements and provide necessary guidance and supervision to those that fail to meet them. Also, provide written guidance to administering agencies regarding follow-up action that should be taken in deficient institutions.

We support the Appropriation Committee's one year moratorium on any additional States turning the administration of the program back to FNS. Additional responsibilities for State program administration tax personnel ceilings at FNS regional offices, detract from mandated monitoring responsibilities and impede effective program administration. While the

Department's Office of General Counsel interprets language in the FY 1981 Agriculture Appropriations Act regarding additional "turnbacks" as permanent in nature, we recommend that such a provision be incorporated permanently into the legislation to clarify this issue.

SUMMER FOOD SERVICE PROGRAM FOR CHILDREN

The Summer Food Service Program for Children was established in 1968 as the summer component of the Special Food Service Program for Children. The program is designed to provide school age children in areas of poor economic conditions with the same nutritious meals as those provided under the National School Lunch and Breakfast Programs during the school year. In addition, mid-morning and afternoon supplements, or snacks, are also provided. Funds are provided to States to reimburse nonresidential public or private nonprofit institutions and residential public or private nonprofit summer camps which develop special programs providing food service to children during the summer and other school-related vacations. The program is administered by the Food and Nutrition Service at the Federal level and, at the State level, by State educational agencies or FNS regional offices. As with the Child Care Food Program, States have had the option of turning the administration of the program over to the Department. The FY 1981 Agriculture Appropriations Act, however, precludes Federal administration of additional State programs for one year. Food and Nutrition Service regional

offices currently administer the program in 19 States. Daily attendance for the peak month of July averaged about 1.9 million in FY 1980. Program obligations for FY 1980 are expected to total approximately \$120.6 million.

The Summer Food Service Program has been plagued with recurring problems and abuses since its inception in 1971. Audits and investigations by both OIG and GAO, and management evaluations by FNS have disclosed widespread abuses such as ineligible and inflated reimbursement claims, spoiled and wasted food, overlapping service areas and meals consumed by ineligible adults. Although regulations have been strengthened each year in an attempt to prevent repetitions of such abuses, they continue to occur. Until the last two years, OIG consistently devoted more staff resources per program dollar to the Summer Feeding Program than to any other area. Between July 1, 1975 and January 31, 1981, OIG investigated 162 cases involving kickbacks, and falsified records, meal counts and claims. Investigative activity during these years resulted in 50 indictments and 37 convictions. Fines, recoveries and collections totaled about \$503,000 for this same period. Approximately \$180,000 in claims were also established and are currently pending collection. These dollar figures do not reflect program payments which have been suspended as a result of program irregularities disclosed by investigations and audit.

We recently completed a nationwide assessment of that part of the 1980 Summer Food Service Program that dealt with the administration of audits contracted for by nonprofit sponsors who expected to receive more than \$50,000 in

program reimbursements. We reviewed State agency and FNS regional office control over 1980 Summer Food Service Program audit requirements and found basically the same problems as we had in an audit conducted one year earlier.

Program regulations require sponsors expecting to receive program payments in excess of \$50,000 (\$75,000 for the 1981 Program Year) to contract with an independent certified public accountant (CPA) or an independent State or local government accountant for an audit of their program. Audits are to be conducted in accordance with OIG and General Accounting Office standards. Sponsors' final claims for reimbursement are contingent upon the completion of such audits and their subsequent review by administering agencies. Our audit sought to determine: (1) whether program audit requirements were being met, (2) whether independent audit organizations can be relied upon to meet USDA audit needs, and (3) the extent to which administering agencies used 1979 and 1980 audit reports in processing sponsor reimbursement claims. We reviewed Summer Food Service Program operations at five of the seven FNS regional offices and at nine administering agencies--five State agencies and four FNS regional offices. Our review also included visits to 78 offices of independent audit organizations under contract to 97 sponsors in the aforementioned nine States. Our audit disclosed that:

- o Both State and FNS administering agencies did not establish or exercise effective controls over independent audit organizations to ensure that audits were conducted in accordance with GAO standards and OIG audit guides. Twelve of the 75 sponsors reviewed in six States began operations prior to engaging an independent audit organization. None of the nine administering agencies reviewed had developed procedures to assess the quality of independent audits. Reviews by administering agencies were confined to superficial desk audits and did not include workpaper or on-site reviews. Thirty-six of the seventy-eight independent audit organizations reviewed were not provided the necessary program materials to perform compliance audits prior to the start of food service operations.
- o Audits performed were generally financial and gave little or no attention to the performance of audit steps necessary to evaluate the program on an ongoing basis.
- o Fifty-three audit reports (62 percent) we reviewed failed to ensure the validity of sponsors' final claims.

The President's proposed FY 1982 budget calls for the elimination of the Summer Food Service Program for Children. However, in the event that the program continues to receive funding, we are negotiating with FNS to assume:

- (1) contracting responsibilities for audit services now performed by FNS, and
- (2) oversight responsibilities for audits performed or contracted by State

agencies. We believe that OIG assumption of FNS contracting and oversight responsibilities will help remedy some of the problems associated with FNS and/or State contract administration that were disclosed in our audit.

As with the Child Care Food Program, we support the Appropriation Committee's one year moratorium on any additional States turning the administration of the program back to FNS and urge that such a provision be incorporated permanently into the legislation.

Dual Funding of Milk in Summer Camps

During our audit of the Summer Food Service Program for Children we found some evidence of dual funding of milk at summer camps participating in both the Summer Food Service Program and the Special Milk Program. In order to more fully substantiate this finding, we selected 12 of the 60 largest summer camps participating in both programs in Pennsylvania, New York, New Jersey and California for audit. We reviewed State agency and/or FNS regional office operations in all four States. Our review covered the months of June, July and August 1979.

The Special Milk Program was established under Section 3 of the Child Nutrition Act of 1966 to encourage the consumption of milk by children in public or private nonprofit residential and nonresidential schools, child care institutions and summer programs. Milk served with meals and supplements is a required and reimbursable commodity under the Summer Food

Service Program. Milk served outside designated meal periods and any second half pint of milk served during a meal period is reimbursable under the Special Milk Program.

Of the 12 summer camps we audited, we found that after applying the camps' total milk purchases to their Summer Food Service Program claims, 11 did not have enough milk purchases left over to support Special Milk Program claims. In addition, three of the 11 camps lacked sufficient milk purchases to fully support their Summer Food Service Program claims. These conditions resulted in overclaims of more than \$40,000 in the Special Milk Program and more than \$52,000 in the Summer Food Service Program.

The Administration's legislative proposals for FY 1982 include a provision to limit participation in the Special Milk Program to those schools and institutions that do not participate in other federally subsidized meal programs. We support this proposal and urge that it be adopted.

Commodity Distribution Program

USDA procures agricultural commodities for use in School Lunch and other Child Nutrition Programs, Elderly Feeding Programs, and Needy Family and Commodity Supplemental Food Programs through the Commodity Distribution Program. The Program is administered by FNS: procurement activities are carried out by the Agricultural Stabilization and Conservation Service (ASCS) and the Food Safety and Quality Service (FSQS). Price support commodities are procured for donation by ASCS under the authority of Section 416 of the

Agricultural Act of 1949, as amended; surplus commodities are procured for donation by FSQS under the authority of Section 32 of the Act of August 24, 1935, as amended. Additional commodities are purchased with funds legislated under Section 6 of the National School Lunch Act.

FNS distributes donated commodities to State distributing agencies who, in turn, distribute them to local recipient agencies; e.g., schools and child care institutions. ASCS is responsible for the administration of all FSQS and ASCS commodity purchase contracts including the issuance of delivery instructions and payments to vendors. Contracts are administered through the ASCS Kansas City Commodity Office (KCCO).

We recently completed a nationwide audit of the program which covered FY 1978-80 commodity operations. We assessed: (1) the effectiveness and efficiency of program planning and procurement activities, (2) the efficiency of the entitlement and distribution system, and (3) the accountability, usage and storage of inventories at State and local school district levels. We reviewed commodity distribution operations at FNS and FSQS headquarters; three of the seven FNS regional offices; the Kansas City Commodity Office; State agencies in Maryland, New York, Massachusetts and Illinois; and nine school districts in the same four States.

Our audit disclosed:

- o FNS did not have a reliable system to identify the commodity needs and preferences of local school districts and State agencies. FNS had not surveyed States on the acceptability of donated foods since

FY 1979. Surveys that were conducted for FY's 1977 through 1979 were incomplete and did not provide FNS with enough detailed information to accurately assess commodity needs. As a result, FNS was unable to fully consider States' overall area preferences and needs in purchase planning.

- o FNS did not have an effective system to monitor inventory levels of donated commodities. Monthly reports submitted by State distributing agencies on the receipt and distribution of commodities were inaccurate, untimely, and/or incomplete and excluded inventories stored at food processors and schools. Six States that had no central warehouses and that subcontracted for commodity distribution routinely reported zero inventories on monthly reports. An additional six States failed to routinely submit monthly reports, precluding a year-end inventory analysis. Moreover, inventories of large cities that act as subdistributing agencies and receive commodity allotments directly from vendors or USDA are not included in State inventory reports.
- o FNS was nine months behind in processing individual State reports as of April 1980. In addition, inventory information was not used to adjust commodity procurement plans or deliveries at FNS headquarters.

- o State distributing agencies reported inventories totaling 210.5 million pounds and valued at \$96.9 million at the close of school year 1979. Since FNS had not defined "excess inventories," we determined that any balance in excess of one month's supply to be a problem at the end of the school year. Approximately 88 million pounds, or \$43 million, of the commodities on hand at the close of school year 1979 exceeded the States' average monthly usage. We estimated that storage and handling costs for these "excess commodities" would total approximately \$920,000 during the non-school months. It should be noted that the above inventory figures and storage costs do not include inventories of commodities delivered directly to the large cities and the 12 States referenced above which account for approximately 30 percent of the program's activities.
- o FNS had not provided detailed instructions to regional offices on the conduct of annual management evaluations of commodity operations at State and recipient agencies, warehouses and processors. FNS subsequently provided regional offices with comprehensive new instructions in FY 1981.
- o FNS regional offices had not performed annual management evaluations of State distributing agencies on a regular basis. We found that 16 State distributing agencies had not been evaluated from April 1977 through April 1980. An additional 29 State distributing agencies had

not been reviewed for one or more years during the same period.

Management evaluations, that were performed, failed to identify significant weaknesses identified in subsequent audits.

Additionally, there was no follow-up system to insure that problems which were identified by management evaluations and/or audits were, in fact, corrected. FNS has subsequently reported that all but one regional office performed management evaluations in FY 1979.

- o FNS had not performed nor did they require ASCS and FSQS to perform cost analyses of different commodity specifications. Purchases of lower grade commodities would more closely parallel commercial products purchased directly by schools and could reduce commodity costs without sacrificing nutrition. Similar savings could also be realized through increased bulk purchases, and canned rather than frozen vegetable purchases.
- o Commodity procurement practices followed by FSQS and ASCS were not consistent or uniform and were not supported by any cost/benefit analysis. Both agencies have different policies on shipping terms required for the delivery of commodities, advance announcement of the quantities of commodities to be purchased, and the use of incremental bidding by vendors.

We therefore recommended that:

- o FNS revise its commodity procurement planning process by obtaining from and providing to States and schools detailed information on preferred commodities and procurement specifications.
- o FNS strengthen the planning process for commodity purchases by giving increased emphasis to the identification and consideration of State and local school district needs and preferences.
- o FNS develop a commodity control system which insures the timely and accurate submission of inventory reports that include information from State subdistributing and recipient agencies and processors.
- o FNS use information on inventory balances to plan future commodity purchases and deliveries.
- o FNS adjust planned purchases to reconcile commodities existing in State and local inventories.
- o FNS develop written guidance to assist FNS regional offices conduct management evaluations. In addition, FNS should develop a system which tracks the compliance of FNS regional offices with annual management evaluations and the implementation of corrective actions.
- o FNS, or FSQS and ASCS, analyze the cost/benefit tradeoffs of providing commodities in bulk form and of a lower grade.
- o FSQS and ASCS conduct an in-depth cost analysis of procurement practices which addresses alternative shipping terms, bidding practices and announcement policies.

RURAL DEVELOPMENT PROGRAMS OF THE FARMERS HOME ADMINISTRATION

We have frequently expressed our concern about the rapid growth in the number and dollar volume of the programs administered by the Farmers Home Administration (FmHA) and the stress this growth has placed on the agency's capacity to manage effectively the expenditure of program funds and provide simultaneously adequate servicing of over \$40 billion in outstanding loan balance.

We have not expressed, as frequently, our concern about the lack of emphasis by FmHA management on the development and maintenance of the management procedures and tools necessary to insure the programs are managed effectively and efficiently. We feel a fundamental reorientation of FmHA management priorities is of absolute necessity if the programmatic problems discussed in this and other reports are to be corrected comprehensively and if the susceptibility of FmHA programs to fraud, abuse and waste is to be reduced significantly.

The mere obligation of program funds cannot in itself be a high priority. Instead, priorities should reflect the careful and comprehensive evaluation of the need for the expenditure, whether all program conditions have been satisfied, and that adequate servicing of the account is provided once the funds are obligated.

While we are of the opinion that some of the management and programmatic problems experienced by FmHA have been caused by personnel shortages, we are also of the opinion that management has failed to analyze thoroughly its

personnel needs and develop specific recommendations regarding the quality and quantity of personnel needed, the allocation of personnel and specific skills in relation to workload, and the short and long term training needs of its personnel.

In general, we feel the agency has failed to view many of the problems reported in our audits as endemic in nature and as having resulted in part from their lack of emphasis on responsible management of the agency's programs, including prompt and thorough corrective action to recommendations in OIG and GAO audit reports.

A particular example of a problem caused by the neglect of the agency's management needs is the failure to develop and implement sufficient financial management information system. The Agency's financial accounting and management systems in the Finance Office are stretched far beyond the capabilities for which they were developed originally in 1966, the impact of which is: (1) financial reports are in error, (2) annual loan statements are incorrect, (3) collections cannot be balanced, (4) the field staff does not have the information it needs to service loan accounts and protect the government's interest in its collateral, and (5) until recently the agency was losing several thousands of dollars per day in interest because transactions were not posted promptly.

Another example is that many of the problems cited in the following discussion of specific audits are recurring problems.

BUSINESS AND INDUSTRIAL LOAN PROGRAM

The Business and Industrial Loan Program was authorized by the Rural Development Act of 1972. The purpose of the program is to stimulate the rural industrial economy by providing loan funds to acquire, construct, reorganize, or expand rural businesses providing new employment opportunities. It is primarily a guaranteed loan program. That is, FmHA can guarantee up to 90 percent of a loan which is usually made by commercial banks. The agency also has authority to make insured (direct) loans to public and private organizations if there is not a commercial lender in the immediate area that is willing to make a loan even though an FmHA loan guarantee is available.

Since the program was implemented in 1973, FmHA has approved 4,962 loan guarantees totaling \$3.5 billion. In FY 1980, FmHA approved 1,160 guarantees totaling just over \$1 billion.

We initiated audit coverage of the program in 1977 and since that time we have conducted 27 audits ranging in scope from a single issue to indepth reviews of program activities. In 1980, we conducted an audit of the decisionmaking processes used in making loans. In addition, we conducted a special impact audit of program activities because previous audits of the program had found several areas of significant program weaknesses including inadequate pre-loan analysis, supervision and servicing of the loan portfolio.

Both the special impact audit and a review of the program by the Surveys and Investigations Staff of the House Appropriations Committee found significant problems still exist in the Business and Industrial Loan processing and loan servicing practices of FmHA. In a report completed recently, the Investigative Staff stated that "Loan guarantees are frequently approved and issued without any indepth analysis, to borrowers who have no reasonable chance of success . . . Policies and procedures are ignored and FmHA officials at both the State and national levels are not aware of the violations or, if aware, unconcerned." The staff also criticized the loan servicing practices. "Approving weak or marginal loans normally requires a strong loan servicing program to avoid excessive losses. Instead of a strong loan servicing program as might be expected, FmHA has a weak program."

It should be noted that in 1979 the Secretary charged OIG and FmHA with the responsibility of developing recommendations to improve FmHA's management controls and lessen the susceptibility of its programs, including the Business and Industrial Loan Program, to fraud, abuse and waste. In October 1980, FmHA initiated action to correct some of the problems by issuing revisions to the Business and Industrial program regulations but the Office of Management and Budget has not yet approved the revisions.

Special Impact Audit

Our review and analysis of 30 statistically selected loans totaling \$97.8 million in 20 States disclosed \$46.6 million of questionable loans to 17 borrowers and \$3.2 million of unauthorized disbursements for 7 borrowers.

We projected that 58 percent of the loans in the universe of 712 loans (loans obligated during FY 1979 and closed prior to January 11, 1980), were of questionable eligibility and that 29 percent of the loans in the universe contained unauthorized disbursements. We are 95 percent certain that the universe of 712 loans, totaling about \$536 million, contains 270 questionable loans of approximately \$79 million. The dollar value of unauthorized disbursements in the universe was estimated at \$52 million for 206 loans.

The most significant problems disclosed are as follows:

Loans Guaranteed for Marginal or Unsound Businesses

We considered 12 borrowers that received \$25,604,000 in loan guarantees to be ineligible for such guarantees. These businesses were in unsound financial condition prior to the loans and the lenders would not have made the loans without FmHA's guarantee. The guaranteed loan funds were used to refinance existing loans of \$9.1 million to eight of these borrowers. Of this amount, \$1 million was used to refinance lender debt in four cases. The lenders' risk exposures were reduced by \$775,176. Inadequate preloan analysis was the major cause for approval of these ineligible loans.

Guaranteed Loans Approved for Questionable Purposes

In our opinion loans were approved for questionable purposes in nine of the loans included in our statistical sample. In eight loans, funds of \$9.1 million were used to refinance debts of unsound businesses. In the remaining loan, a \$14,276,250 loan guarantee for one borrower had been

approved for purposes of questionable eligibility, such as transfer of ownership and debt refinancing without creating or maintaining jobs and for purchase of a business in an urban area.

Inadequate Collateral and Collateral Appraisals

We considered that loans to eight borrowers in our sample were inadequately secured in relation to loan value because of disposal of proposed security property prior to loan closing; acceptance of intangible assets of questionable value; inadequate analysis by FmHA of collateral value; and inadequate collateral appraisals. Prior appraisal reports prepared by independent fee appraisers had not been obtained as required on property serving as collateral on 11 loans totaling more than \$31 million.

Insufficient Equity

In 11 instances we considered guaranteed loans totaling \$22,994,000 did not meet FmHA's 10 percent minimum equity requirement as prescribed in the program regulations. FmHA used items such as appraisal surplus, subordinated debt, and personal or outside assets to bolster borrowers' net worth to meet the equity requirement. We believe these type values cannot be reflected on the balance sheet.

Inadequate Monitoring of Loan Closing and Lender Servicing

Inadequate monitoring of loan closings and lender servicing by FmHA continues to be a serious problem in the management of this program. In 18 of the 30 loans reviewed, State office officials were providing little or no

supervision of loan closings and lender servicings. In seven of the 18 loans we found unauthorized or questionable fund disbursements of about \$3.2 million. The magnitude of the problem became apparent when this factor was projected statistically to our sampling universe of 712 loans. Improper disbursements were projected in 206 loans amounting to about \$51.7 million.

Overstatement of Program Accomplishments Based on Inaccurate Job Data

FmHA does not have an adequate system to determine the accuracy and reasonableness of the reported number of jobs created or saved by the B&I program. Consequently, information provided to Congress relative to the number of jobs created or saved through the program has been overstated. FmHA reported to Congress that 180,527 jobs were created or saved from the program's inception through September 30, 1979. The number of jobs reported was based on applicants' projections for obligated loans. The 30,369 jobs projected to be created or saved from FY 1979 loans to the 712 borrowers in our sample were overstated by about 17,769 jobs (59 percent). Furthermore, we identified an additional 18,000 jobs reported as being created or saved since program inception although the loans were deobligated and never made.

Additionally, we found instances of conflict of interest between the borrower and lender; excessive guarantee percentages; lack of legally sufficient provisions for withdrawing conditional Commitments for Guarantee; and weakly drawn terms in Lenders' Agreements making them unenforceable in the event of negligent lender servicing.

We made the following recommendations to FmHA:

- o Emphasize to program personnel the importance of adequate pre-loan analysis.
- o Clarify and properly define vague instructions and terms relating to applicant ability.
- o Require applicants to submit audited financial statements.
- o Instruct the program staff to obtain sufficient collateral based on independent appraisals; refrain from using equity values that provide no real financial stability to the applicant; obtain independent feasibility studies reflecting the economic, market and technical viability of the projects.
- o Strengthen the Conditional Commitment for Guarantee and the Lender's Agreement by specifying those conditions on which the Commitment can be withdrawn and by defining and specifying what is acceptable and negligent loan servicing.

BUSINESS AND INDUSTRIAL LOAN PROGRAM IN THE STATE OF OKLAHOMA

At the request of the Farmers Home Administration, we conducted an audit of the Business & Industrial Loan program in Oklahoma. The request for our assistance followed a national office review of program operations in Oklahoma in which several program deficiencies were noted.

The audit disclosed that the State office had not adhered always to basic B&I program policies, procedures and regulatory requirements. The following are some of the more significant problems disclosed:

Loan Processing and Approvals

Loan funds were obligated consistently before the State Loan Review Board had reviewed the applications. This occurred in 57 of the 77 loans reviewed. In 28 instances, loan funds were obligated prior to the receipt of the formal application and in two instances conditional commitments on the loan were issued prior to the receipt of the formal application.

In other words, the State office was obligating the loan funds prior to having reviewed, or in some cases received, the documents from which they could determine financial or technical feasibility of the project.

Borrower Equity

Twenty-seven of the 77 borrowers received loan guarantees totaling about \$10 million even though they did not meet the 10 percent minimum equity requirement suggested by FmHA program instructions. The State office accepted intangible assets, surplus appraisals, and subordinated debts to increase the borrowers' equity position to meet FmHA requirements.

Improper or Questionable Loan Purposes

In twenty-six loans with a total value of \$10 million the loan purpose was of questionable propriety. Contrary to FmHA instructions, four of the loan guarantees were used to refinance (bail out) the lenders' marginal or high risk loans. As a result, the lenders' aggregate risk exposure on these loans was reduced by \$927,102. In addition, six loans were used to transfer ownership of the business even though there was little evidence indicating

whether the business would have closed or that jobs would be lost had the loan guarantee not been approved; two loans were used for ineligible purposes (i.e., one was an investment venture and the other was located in an urban area); the loan purpose was misrepresented in 9 cases; and revolving lines of credit were established in 5 cases.

Each of the above purposes is either prohibited or discouraged by the Act or regulations.

Improper Expenditure of Loan Funds

Loan funds totaling approximately \$2.6 million were used to pay obligations to persons or entities having equity in the businesses for which the loan guarantees were issued; used to pay non-business related debts, and various other unauthorized purposes such as making loans to individuals, purchasing certificates of deposit, and repaying the bank note on a personal automobile loan.

Loan Security

There was inadequate loan security or inadequate collateral appraisals for 16 loans totaling \$8.3 million. In many cases the value of the collateral was grossly inflated.

Conflicts of Interest

A conflict of interest existed in nine of the loans reviewed. In the majority of the cases principles in the firm seeking the loan were also principles or stockholders in the lending institution.

Compensating Balances

Contrary to FmHA regulations two lenders required borrowers to maintain compensating balances to eliminate or further reduce the lenders risk exposure on the unguaranteed portion of the loans.

Loans to Independent Trucking Corporations

As an adjunct of the audit of the Business and Industrial Loan Program in Oklahoma, we audited loans made to independent trucking corporations in that State. The loans were audited separately because of (1) the volume and unique character of the loans, and (2) serious concerns expressed by the FmHA National Office staff regarding the methods by which the loans were approved.

In 1976, a trucking firm submitted a pre-application for a \$5 million loan guarantee, the purpose of which was to refinance equipment debts and to purchase additional equipment. The FmHA National Office discouraged approval of the guarantee because of (1) insufficient equity, (2) the ratio of debt to net worth was too high, and (3) there was no reasonable assurance of repayment ability.

The following year a director of the firm and the president of a local bank developed an individual owner/operator financing plan under which the owner/operator of the truck would (1) incorporate, (2) provide an initial capital investment of \$500, (3) execute a transportation service agreement

between the new corporation and the truck firm, and (4) execute a management agreement (including power of attorney) which granted overall management control of the corporation to a resident agent.

The director of the truck firm divested his interest in the firm and became the resident agent of the individual owners/operators. His responsibilities included accounting and general financial management services. The truck firm would furnish trailers, freight loads and schedules, maintenance and extend to the new corporations a line of credit to be used as working capital and to make loan payments to the lender.

The lender then submitted a loan guarantee application to the Small Business Administration which rejected the application on the grounds that the owner/operator of the truck was not able to control his own truck which was the collateral of the loan nor was the owner able to write checks on the business account. The SBA was of the opinion that the individual owners/operators were merely instruments to further the business interest of the truck firm.

The lender then submitted the application to the FmHA state office which accepted the plan and by January 1980 had approved loan guarantees totaling \$2.6 million for 92 borrowers.

The audit disclosed the following:

- o The primary reason for developing the financing plan was to limit the original applicant's liabilities for equipment and increase cash flow.

- o The plan created new jobs only at the expense of eliminating 60 formerly independent owners/operators who had previously supplied the firm with both trucks and trailers.
- o The lender received significant yields on the loan guarantees by selling the guaranteed portion on the secondary market. The average yield received for the seven loans in our sample was in excess of 24 percent.
- o The primary purpose of the plan, as advanced by the lender, was to enable individual truckers to become owners/operators. However, of the 83 currently active FmHA backed corporations 65 (78 percent) are now effectively owned and controlled by the resident agent.
- o Some of the loan guarantees were used to refinance existing indebtedness on old trucks rather than purchasing new trucks as was stated on the applications.

We made the following recommendations to the FmHA state office:

- o The practice of accepting subordinated debt to enhance borrower equity should be discontinued.
- o Discontinue the practice of guaranteeing loans to corporations or other entities not having effective control over the day to day operations of their businesses.
- o Assure that collateral is physically inspected and appraised by qualified appraisers.

Alcohol Fuel Projects

In our previous semiannual report we pointed out that we had audited the decisionmaking process in the Business and Industrial Loan Program because of concerns voiced by persons within FmHA, the Office of Inspector General, the Secretariat, and from outside the Department. We were concerned not only with the issue of whether or not external pressures were leading to the approval of business and industrial loan guarantees for reasons unrelated to the financial and economic feasibility, but also with the appearance that external political or other pressures were factors in the approval of such loans. As we reported, in the 40 loans reviewed there was a considerable amount of external involvement in the loan-making process. We also reported that while this did not mean that all the loans reviewed were not worthy of being approved, it did highlight the fact that these loans could have been approved for reasons other than financial or economic feasibility.

Based on the audit we made several recommendations to the Secretary to improve the Business and Industrial loan decisionmaking process. Although the agency agreed to make the recommended changes in the decisionmaking process and adhere to decisionmaking policies and practices previously approved, a recently completed audit suggests that there are still serious deficiencies in this decisionmaking process.

In early August 1980, FmHA had not obligated approximately \$450 million (41 percent) of its FY 1980 Business and Industrial Loan Program authorization. The FmHA national office management decided to use a large portion of these funds to guarantee loans for energy-related projects in order to assist in meeting the Administration's annual production goal of 500 million gallons of alcohol fuels by the end of 1981. Between September 5, 1980 and October 8, 1980, 15 loan guarantee applications totaling about \$342 million were reviewed and obligated by the FmHA national office.

Our review of each of the 15 loan guarantees revealed the following:

Improper Loan Processing and Approvals

Improper Obligations

Our review of the 13 loan guarantees totaling \$217.8 million, approved from the FY 1980 authorizations, disclosed that all of the loans were improperly obligated. FmHA did not complete the proper steps in the decisionmaking process prior to the end of the fiscal year. Consequently, FY 1980 funds could not properly be used for the projects.

Contrary to the recommendations we had previously made, and the Agency had agreed to implement to strengthen the decisionmaking process, we found that the Under Secretary for Rural Development was apparently directly involved in the approval and disapproval of the loan guarantee applications. We also found that:

- o loan processing procedures were disregarded or violated,
- o the applications were not adequately evaluated for technical and economic feasibility,
- o the level of loan guarantee was not negotiated in relation to risk exposure, and
- o "outside" contacts from other than FmHA employees and lender/applicant representatives concerning the applications were not always documented.

In rushing the processing of these loan guarantee applications, FmHA violated or caused violations of several of their regulations and procedures, including arbitrarily waiving environmental impact statements for most of the proposed projects without sufficient support for such determinations. In several cases, State offices were given less than 24 hours to analyze thoroughly the environmental impact of the projects and determine whether or not an environmental impact statement would be needed.

Inadequate Pre-Loan Analysis

The evaluation of project feasibility by State and national office personnel did not adequately ascertain the economic feasibility of the 15 proposed alcohol fuel plants. Our review disclosed that factors such as demand for gasohol, affect of other competitors, potential grain shortages and rising grain prices, reasonableness of project costs, cost in loan funds per job

created (from a low of \$188,235 to a high of \$903,486), and the inexperience of management in ethanol production; were not addressed during FmHA's review of these applications.

Inadequate Feasibility Determinations

FmHA relied on its Environmental and Technology Staff to evaluate the feasibility studies submitted as part of the 15 applications. However, this staff: (1) is inexperienced in ethanol production, (2) performed checklist, cursory type reviews, and (3) did not analyze cost or economic feasibility. We found that: (1) the resolution of the staff's numerous exceptions with these feasibility studies were not always documented, (2) there was no documentation of such reviews for six projects, (3) the feasibility study was not considered independent or adequate for at least 12 projects, and (4) five of the engineering firms, who prepared these studies, had little or no experience in ethanol production.

Questionable Loan Purpose

Ten of these projects could have been funded through the program created by the Energy Security Act of 1980 had FmHA waited a few days and processed the applications under this new authority. Five of the 15 projects, however, still would not have been eligible because the Energy Security Act required that any project anticipating an annual production capacity of more than 15 million gallons would have to be financially assisted by the Department of Energy. Five of the projects approved by FmHA had an annual production capacity exceeding 15 million gallons.

Borrower and Lender Risk

Our review and subsequent interviews with lenders revealed:

- o FmHA processed loan guarantees at the maximum 90 percent of the loan amount in 14 cases, despite the risk involved in such an unproven industry. FmHA instructions state that consideration should be given to reducing the guarantee when higher risk is evident.
- o Some lenders were unwilling to retain one-half of the unguaranteed portion of the loans, as is now required, because of the high risk.
- o Borrowers' risk was limited to their initial investment through limited partnerships or corporations because there was no requirement for personal guarantees.

In ten projects, the applicants offered no personal guarantees for the loans and the individual principals' investment risk was not limited by partnerships or corporate structures. In seven of the ten, personal guarantees were not required by FmHA. In four cases, the personal guarantees were limited to the amount of their initial investment which was usually far less than the loan.

On January 27, 1981, the Secretary ordered that further processing of alcohol fuel loan guarantees be stopped pending a re-evaluation of the applications and supporting documentation. From February 13 to February 20, 1981, an independent review committee consisting of three State business and industrial loan program chiefs not involved with the 15 projects, reviewed

the applications and related files to determine if the applications could be further processed. This team recommended that 12 of the applications be returned to the State offices for additional processing because of major defects relating to the economic and/or technical feasibility of the projects. The team recommended proceeding with the remaining three projects after a review by the State Directors and the issuance of additional conditions for the Conditional Commitments for Guarantee. In addition, FmHA deobligated the 13 loan guarantees totaling \$217.8 million which were obligated from the FY 1980 B&I authorization.

Presently, eight of the 15 loan guarantee applications have been resubmitted by the State offices to the FmHA national office for review and approval. Five of the eight are presently being evaluated by the loan review committee. The remaining seven applications are still being reprocessed by the appropriate State office.

COMMUNITY PROGRAMS

The Community Programs administered by FmHA originated in 1937 as a water supply program for 17 western States. The Consolidated FmHA Act of 1961 expanded the program to the general rural population and in 1965 changes permitted a loan and grant program for both water and waste disposal systems. The Rural Development Act of 1972 authorized the use of FmHA loans for essential community facilities such as fire departments, libraries, hospitals, and other necessary facilities.

Community program loans must primarily serve farmers, ranchers, farm tenants, farm laborers, or other residents of open country and rural towns and villages having a population of not more than 10,000. Recent legislation has raised the population limit to 20,000 for community facilities loans. The loans are repayable in 40 years and bear an interest rate of five percent. In FY 1980, loans and grants made for water and waste disposal systems and other community facilities totaled \$1.2 billion.

Using statistical sampling techniques, we randomly selected 47 of 378 loans of over one million dollars for review. Total funding from all sources (FmHA, other Federal agencies and State and local agencies) on the 47 projects was \$215.7 million of which \$142 million was FmHA loans and grants.

In general, the audit disclosed that FmHA had not exercised adequate management controls during project development and planning. There were 34 instances in which we considered the projects to be: (1) either of questionable eligibility because they were serving urban residents, (2) the design capacity substantially exceeded projected need, or (3) excessive costs were caused by inadequate planning, construction delays or operational problems, and (4) unauthorized use of funds. These problems resulted in \$13.7 million in questionable or excessive expenditures. Some of the specific problems were as follows:

Projects Serving Residents of Urban Areas

One applicant received an FmHA grant of \$3 million and an FmHA loan of \$3.7 million to install a waste water collection system and treatment plant. The service area is an urbanized resort community consisting of two islands adjacent to Ft. Myers Beach, Florida. FmHA records show that the permanent population of the service area before the loan and grant were approved was 12,014 with an additional 12,000 tourist population. Houses and condominiums in the area sell for approximately \$100,000 and rent for as much as \$500 per week.

While we agree that the project according to FmHA regulations was technically eligible for FmHA assistance, we believe its priority should have been so low compared to other projects that the issuance of the loan, and more important the grant, should not have been approved.

Excessive Capacity

Three of the 47 projects were designed and constructed with capacity in excess of need at an approximate cost of \$3 million because FmHA did not actively monitor the capacity or scope of the project. For example, one project when initially proposed was to upgrade the water treatment and storage capacity from 1 to 2 million gallons per day. Project justifications showed that this expansion would provide sufficient capacity for the next 20 years. When a contract underrun of \$400,000 occurred the city applied for

and obtained without sufficient justification an additional \$135,000 loan and used the \$535,000 to further expand its water treatment and storage capacity to 4 million gallons per day.

Planning and Operational Problems

Inadequate planning and subsequent operational problems led to deficiencies in eight of the 47 projects which may cost the borrowers an additional \$800,000 to correct.

Construction Deficiencies and Delays

Delays in project construction and poor construction quality resulted in increased costs of over \$680,000 on eight projects.

On one sewerage project, disputes between the equipment supply and installation contractors resulted in delays and extra legal and engineering costs. Eight of 203 tanks collapsed during testing and were replaced at the borrower's expense. The resident inspector determined that the walls of the tanks were one-half the width specified and the manufacturer had switched the material composition of the tanks. As a result of the tank failure project completion was delayed, legal and engineering fees have increased and there may be additional operational problems because the other 195 tanks do not meet the original specifications. This issue is now in arbitration.

Excessive Engineering and Legal Fees

FmHA did not adequately monitor payments to project engineers and attorneys and as a result approved about \$200,000 in fees that either were in excess of the fee specified in the agreements or were based on the wrong fee schedule.

Premature Advance of Funds

A lump sum advance instead of multiple advances were used on two projects. The additional interest expense to the Government was about \$142,000 for the funds advanced that were not needed by the borrowers.

Change Orders

In 11 of the 47 projects, deficiencies were noted in justifying, submitting, and approving orders changing the scope of the project. In eight instances, change orders totaling \$388,000 were not approved and in other instances change orders totaling \$591,000 were questionable.

Lack of Control Over Unobligated Balance

FmHA had over \$142 million in outstanding obligations (funds that were not being utilized) at the time of our review. We determined that over \$11 million of the funds were not needed and could be deobligated. In some cases, FmHA permitted some of these funds to remain obligated for 10 years.

We made the following recommendations to FmHA:

- o Assure that loans and grants benefit primarily rural residents by revising FmHA instructions regarding eligibility to require that the most current population and income information be used when it is known that significant changes have occurred since the last decennial census.
- o Assure that pressures to obligate funds and approve projects and required contracts do not override the need for a thorough project review and analysis.

- o Counsel applicants regarding problems that may occur. Assure that applicants are aware of their obligations and responsibilities.
- o Monitor construction progress, perform necessary inspections and review closely relevant project documentation.
- o Increase management controls over program funds. Specifically: deobligating funds when they are no longer needed; transferring funds to borrowers only as needed; and insure that program funds to be used only for authorized purposes.

FmHA has agreed to implement the recommendations.

EVALUATION OF LOAN SECURITY AND REPAYMENT ABILITY

This audit was conducted to determine if FmHA's security for farm operating type loans was obtained and serviced in accordance with relevant laws and regulations. These loans (operating, emergency, and economic emergency) comprise about 73 percent of all farm program loans made by the agency. As of May 1980, there was over 174,000 borrowers with farm operating type loans. The unpaid balance of those loans was \$12.3 billion. On September 20, 1980, approximately 119,000 loans with a loan balance of \$3.8 billion were delinquent. The delinquent portion of these loans was approximately \$930 million.

Operating loans provide short to intermediate term production or chattel credit to farmers who cannot obtain credit elsewhere. The repayment term is usually for seven years and renewable for up to an additional seven years. The interest rate is the government's cost of borrowing money (currently 13 percent).

Emergency loans are made to farmers in designated disaster areas for the purpose of restoring production. Farmers unable to obtain commercial credit are eligible for actual loss loans up to \$500,000 per disaster at an interest rate of 5 percent. Credit-worthy borrowers can also obtain actual loss loans up to \$500,000 per disaster but the interest rate is the government's cost of borrowing. Annual production and major adjustment loans may also be made with interest rates equal to the government's cost of borrowing.

Economic emergency loans are made to farmers and ranchers who are primarily and directly engaged in agricultural production and who are experiencing economic hardships due to credit scarcity or a cost/price squeeze. Operating loans carry current interest rate of 13 percent and are repayable in seven years and can be extended up to a 20 year period. Loans for real estate purposes can be made for periods not to exceed 40 years. The current interest rate is 12.25 percent.

We statistically selected 100 of the 174,641 borrowers for our review. The unpaid loan balances for the borrowers reviewed was \$7.1 million and for all active borrowers \$12.3 billion.

The two major findings were borrowers had disposed of loan security without FmHA's knowledge; and borrowers did not have long-term debt repayment plans or adequate repayment ability. Specifically the audit disclosed the following:

Unauthorized Disposition

Twenty-two of the 100 borrowers in our sample had disposed of mortgaged property (real estate, crops, chattel) without FmHA's knowledge. These borrowers had unpaid loan principal balances totaling approximately \$993,000. In eleven of the 22 cases the remaining loan security was inadequate to cover the loan principal balance. Borrowers have little difficulty in selling FmHA security, particularly crops and livestock, and using the proceeds for unauthorized purposes. FmHA procedures to prevent unauthorized disposition depend heavily on the integrity of the borrowers and action taken against borrowers who make unauthorized dispositions.

Actual deterrents are limited primarily to farm visits to inspect crops and chattel, notifying buyers in the local trade area of FmHA liens on the borrowers' crops and chattel; taking action such as liquidation against borrowers; and taking action to recover funds from buyers of security under FmHA liens. The deterrent procedures are not effective, however, unless they are pursued vigorously.

In many of the cases reviewed, FmHA personnel did not conduct the required inspections to check the loan security and did not notify local traders of FmHA liens on various property. Generally, FmHA officials attributed the lack of inspections and other preventive measures to inadequate staffing.

On the basis of our sampling plan we projected (with 95 percent confidence) that 36,872 of the 174,641 borrowers have disposed of loan security and that approximately \$1.4 billion in loan principal is, by FmHA's definition, to some degree in jeopardy. This is not to suggest the possible loss of that amount of money but rather to indicate the extent of the problem of unauthorized disposal of property mortgaged to FmHA.

Lack of Repayment Ability

Twenty-seven of the 100 borrowers in our sample, with unpaid principal balances of \$2.1 million, did not have realistic plans for long-range debt retirement. Twenty of the loans were delinquent by a total of \$506,000 in payments. We projected, with 73 percent confidence, that the farm plans for 39,141 borrowers with unpaid loan balances of \$3.2 billion do not provide for ultimate repayment of current and future loan obligations because: (1) the present market value of the collateral is not equal to the amount of the loan, (2) all of the borrower's debts were not considered in the farm plan, or (3) agency policies limiting foreclosure or denial of credit.

FmHA instructions for the operating, emergency, and economic emergency loan programs state, in part, that if the present market value of the collateral is not at least equal to the amount of the loan, the applicants' repayment

ability may be considered by the loan approval official in determining whether the loan should be made. When repayment ability is considered, it will be on the condition that the typical year operating plans indicate ability to pay the loan in full within the proposed payment period.

The instructions do not give consideration to all of the borrowers debts. Our interviews in 10 State offices and with 29 County Supervisors disclosed different interpretations of repayment ability. Some of the officials were of the opinion that a borrower has repayment ability when the farm plan shows that all debts, including FmHA and other creditors, can be paid as scheduled; others stated that if all debts could not be repaid, then old debts could be refinanced, rescheduled, or remortgaged, or in the case of debts to other creditors nondisturbance agreements could be obtained; others told us that a borrower has repayment ability when the farm plan shows that current operating loans can be paid in full and that interest or partial payment can be made on older loans.

The agency has encouraged liberal loan making policies. An administrative announcement issued in January 1978 stated that under no circumstances will a farmer be foreclosed or denied credit if otherwise eligible where there is a reasonable chance that he can remain on the farm.

Recommendations

We made the following recommendations to FmHA:

- o Strengthen and enforce instructions by requiring an annual inspection of crops and chattel securing all operating farm loans.

- o Require lists of borrowers to be furnished to business firms that normally buy or sell chattel.
- o Instruct State offices to emphasize to borrowers their responsibilities of obtaining FmHA approval before disposing of FmHA loan security and vigorously pursue civil or criminal action against borrowers who dispose of such security as well as against third-party converters.
- o Amend regulations and instructions pertaining to operating type loans to require the preparation of realistic long-range plans including repayment ability for each applicant.

DEPARTMENTAL ADMINISTRATION

During the reporting period we increased our audit coverage of the administrative systems and operations of the Department. During the past six months we have completed audits of claims collection policies and procedures, continued our efforts in the procurement field, and started audits on some of the major financial priorities areas, such as debt management, internal controls, and cash management. We are doing substantial audit work on ADP systems, and monitoring systems development, with emphasis on ADP security.

USDA TRAVEL MANAGEMENT

We recently conducted a survey of travel management within USDA to assess the overall management of travel expenditures within the Department and to evaluate the effectiveness of Departmental efforts to reduce travel expenditures during FY's 1979 and 1980. Our review included discussions with officials of the Office of Budget, Planning and Evaluation, the agency which handles USDA's budget, the Office of Operations and Finance which obtains information on expenditures and has oversight responsibility for Departmental travel, and seven of the agencies with the largest travel budgets. We also sent questionnaires to 12 additional agencies, and reviewed applicable budget and expenditure data for all Departmental agencies.

We concluded that the Department needs to establish more specific priorities for the allocation of travel funds to better insure that the most essential programs and activities requiring travel will be accomplished during periods

of budgetary constraints. In this regard, travel reductions for FY's 1979, 1980, and 1981 have been accomplished primarily by across-the-board reductions based upon budgets or prior years' expenditures rather than established program priorities.

We also noted that USDA financial management systems, internal controls, and management accountability have not been adequate to insure that required travel budget reductions have, in fact, been accomplished. Specifically, in FY 1979 and 1980 when travel ceilings were imposed, USDA overspent the ceilings by \$9.2 million and \$9.4 million respectively, or approximately 7 percent each year.

CONSULTANT SERVICES

Our previous semiannual report included highlights from an audit of consultant service contracts which recommended that sole-source procurements need to be closer controlled and that the Department inform all administrators of the general findings and recommendations contained in our report, emphasizing that: (1) justifications showing that in-house capabilities are not available must be reasonable, proper, fully supported, and adequately documented; and (2) procurements, especially those made in the last quarter, must have documented justifiable need and be awarded in accordance with prescribed procurement regulations. We have worked closely with the Office of the Assistant Secretary for Administration in developing a plan for the control of consulting services and the improvement of procurement practices within the Department.

In response to our recommendations, the Department will shortly issue a directive which will provide a more complete definition of sole-source procurements and will delineate the responsibilities of personnel involved in the acquisition process. Included in this directive will be the requirement to synopsise all sole-source requirements in the Commerce Business Daily to serve as adequate documentation for the justification of the sole-source procurement. It further emphasizes that contracts in excess of \$10,000 shall not be negotiated on a non-competitive basis without prior review at a higher level than the Contracting Officer. The Department has also established Contract Review Board procedures which will include a review of sole-source contracts over \$10,000 for consulting services, services from former employees, and unsolicited proposals.

The Department's Management Control System for Consulting Service Contracts and Improvement of Agency Procurement Practices as approved by the OMB has been finalized. We will evaluate the system's effectiyeness after it has been implemented.

One of the major problems found in our audit was that there was not a clear understanding of what constituted consultant services. Many of the problems described in our report had to do with procurements that did not meet the strict OMB definition of consultant services. We understand that OMB is in the process of revising its policy to require that the management control system for consultants be applied to related areas such as management and

professional services and special studies and analyses. Since OMB is in the process of revising policy, the Assistant Secretary believes and we agree that it would be premature to expand the Department's definition and use of the management controls. We will continue to monitor the Department's efforts to strengthen the consultant procurement practices.

YEAR-END SPENDING

We are currently conducting an audit of year-end spending. We have analyzed data obtained from the Federal Data Reporting System and have selected 15 procurement offices with year-end spending surges; audit emphasis will be given to contracts awarded on a noncompetitive basis.

The objectives of the audit are to evaluate the effectiveness of procurement management within the Department through a review of year-end transactions and determine whether year-end transactions are supported and satisfy a bona fide need of the current fiscal year, and will evaluate overall procurement planning, performance of personnel, monitoring of contract performance, and the delivery and use of final products.

As part of our overall audit effort in this area, we have to date reported on the following:

FmHA Contract The Farmers Home Administration contracted for the performance of a National Rural Community Facility Assessment Study to acquire reliable data about existing rural community facilities, the degree of national need for these facilities, and an estimate of the cost to meet this need. The

contract was awarded on September 28, 1978, for \$3.1 million although total costs were expected to be between \$4 and \$5.5 million. Phase I of the contract included development of the data collection plan, standards by which to assess the data, and alternative approaches to performance of the study in Phase II. Phase II would entail the actual collection and analysis of data.

Our review disclosed that the contract was awarded at year end without a clear understanding by FmHA of the work to be done or how the results would be used. Delays in reaching major decisions, such as whether the contractor was to provide national or State estimates, and the sample size for Phase II, proved to be very costly. By March 1980, \$4.5 million had been obligated, and another \$4.6 million was needed to complete the study. We reported our concerns regarding procurement weaknesses to the Secretary and recommended several alternatives for completing the project.

Plum Island Construction Project A contract was awarded by the Science and Education Administration (SEA)* for the construction of additional laboratory facilities on Plum Island, New York. The contract was awarded September 24, 1976, and totaled approximately \$11 million.

Extremely low quality work caused delays in the construction, leading to default in March of 1979. The major problems were:

*SEA was formed in October 1977 to include the Agricultural Research Service which awarded and managed the contract through most of its life.

- o Work in place damaged by neglect or exposure to weather;
- o Improper installations requiring correction or replacement;
- o Questionable adequacy of certain construction features to achieve the goals of the program.

Since SEA intended to request an additional \$15 million to complete the facilities, the Senate Appropriations Committee requested us to evaluate the adequacy of the management of the original contract. Our review found that problems existed in the administration of this contract beginning with the planning stage and continuing up to the termination of the contract. The problems included: (a) contract award under "hurry up" pressure before the end of the year; (b) a superficial credit and responsibility check even though there was information available that the contractor had not satisfactorily completed other government contracts; (c) inadequate monitoring by regional and headquarters personnel; (d) partial payments which exceeded allowable amounts (contractor receiving approximately 80 percent of the contract amount when only 58 percent of the work was completed); (e) progress payments paid in full with no deduction for defective work noted by construction inspectors; (f) waiver of the retainage fee when it was known that subcontractors were not being paid properly; and (g) approval of change orders with inadequate supporting documentation and without a determination of the reasonableness of costs.

Our review also disclosed that key officials failed to take corrective action when severe problems occurred. Despite delays (including a five-month delay in start-up) in construction and unacceptable work the contract was not terminated until 14 months after conditions noted in January 1978 made it obvious that the contractor would be unable to complete the project satisfactorily.

After receiving our report, SEA and the Office of Personnel requested that we conduct an investigation of the responsible individuals involved. This has been completed and the report has been submitted to SEA to determine the extent of disciplinary actions against responsible personnel.

In addition, in October 1978, OIG began an investigation into possible fraud at the request of an SEA contracting official. In February 1981, the contractor was found guilty of inflating costs in job change orders. In April 1981, the contractor was sentenced to 18 months imprisonment and he and the construction company were each fined \$45,000. It has also been determined that the contractor's surety company is liable on a \$10 million performance bond to complete the project.

Cotton Classing System As part of our systems procurement survey, we found that the Agricultural Marketing Service (AMS) did not have adequate documentation justifying a proposed acquisition of 14 minicomputers costing about \$480,000. AMS plans to use the minicomputers as a test for automating the recording of cotton classing information. Our analysis of the AMS proposal found no evidence that they fully explored all available

alternatives or conducted studies to support their requirement for total on-line data storage. Further, the results from prior years' tests of cotton classing automation had not been sufficiently analyzed. It is our opinion that use of one of the Department's computer centers would be a viable and possibly more economical way to meet AMS' needs. Discussions with AMS regarding our findings are continuing.

DEBT MANAGEMENT

A Department task force has been studying debt management problems, practices, and procedures under the direction of the Assistant Secretary for Administration. The five agencies (Commodity Credit Corporation, Farmers Home Administration, Forest Service, Rural Electrification Administration, and Federal Crop Insurance Corporation) with the majority of the Department's debt were included in a Phase I study released in 1980. A Phase II task force review of debt management by the Food and Nutrition Service, Food Safety and Quality Service, Soil Conservation Service, and the National Finance Center is currently underway. We have worked closely with the Office of Operations and Finance, the lead agency, throughout this effort.

We are now conducting an audit which will concentrate on agencies with substantial accounts receivable due from the public. The objectives of the audit are to determine if:

- o The recommendations of the debt management task force are being implemented.
- o Additional improvements in debt management procedures are needed.
- o Debts are being accurately and timely recorded.
- o Applicable laws and regulations are being followed.
- o Interest is charged on overdue accounts.

CASH MANAGEMENT

Cash management has become an ever increasing concern within the Federal government due to the increased cost of obtaining money and the large volume of cash transactions. Cash management rules, regulations, and procedures have been strengthened to encourage more efficient management of cash.

The Department established a cash management review task force in 1978 which reported that as a result of programs implemented and decisions made by USDA, interest costs should be reduced by nearly \$17 million in FY 1978. When existing plans were fully implemented, annual interest costs were expected to decrease by a total of \$30.3 million in future years. The major areas contributing to these savings were: (1) better timing on the disbursement of loan and grant funds; (2) depositing collections at a local level; and (3) consolidating functions for more timely billings.

Although the Department has emphasized cash management, recent audits have noted a need for improvement in most agencies' cash management programs. The more serious problems concern:

- o Keeping cash disbursements to the minimum required, at any point in time, to reduce the cost of Treasury borrowings. We found that the multiple advance feature of one agency's disbursement system was not effectively used. Because amounts were withdrawn in advance of needs, we projected excess annual interest costs of \$20 million.
- o Delays in depositing cash or systems which prevent the prompt deposit of cash payments. A recent audit showed that in one agency \$1.4 million could be saved for each day eliminated between the date of collection and deposit (current average delay was 8 days).

We are currently conducting an audit of cash management within the Department which will, among other things, follow up on problems noted by the USDA cash management review task force and prior audits to determine if recommended improvements were accomplished.

INTERNAL CONTROLS

The significance of this area has been demonstrated by a recent Congressional proposal for legislation which will require agencies to improve their systems of internal accounting and administrative controls. In recent years, the government has experienced a number of illegal, unauthorized, and questionable payments because of various abuses of current operating systems. The Department's Office of Operations and Finance and the Office of Inspector General have recently initiated efforts to study internal controls within USDA.

We are currently conducting an audit to ascertain if the Department has taken action to institute controls in accordance with the latest OMB guidelines. We have initiated survey work for this audit by reviewing prior OIG audit reports that identified weaknesses in agencies' internal control systems in the areas of Security of Property and Records; Separation of Duties; Reconciliation Procedures; Duplicate Loan Issuances; and Recording of Accounts Receivable.

Audit Follow-up

Our previous semiannual report cited our audit of the Food and Nutrition Service's (FNS) system to establish and collect claims for program losses reported by audits. We measured the agency's system against the requirements promulgated by the Department, OMB, and the Federal Claims Collection Act of 1966. In general, these requirements are that a claim determination be made within six months for any losses cited in OIG reports and that prompt action be taken to collect or otherwise resolve established claims.

At the time of our review, FNS records listed 357 OIG reports (of which 87 were released prior to 1977) containing potential claims totaling about \$60 million for which a claim determination had not been made, or if made, the amount due had not been collected or properly resolved.

FNS agreed to implement our recommendations and together we undertook a concerted effort to resolve these longstanding audits. Each of our Regional Office staffs held working sessions with their counterpart FNS Regional

Office staffs. The meetings were designed to identify those audit issues that were not resolved and to develop corrective action plans with tight time frames for completion of the corrective action. Similar sessions were held by the OIG and FNS headquarters staffs on those audits requiring headquarters assistance or where legal advice was needed from the Department's General Counsel.

The meetings have been highly successful and, pending completion of corrective action plans, we will be able to close most of the longstanding unresolved audits in the very near future.

We plan to continue monitoring the audit resolution process by FNS as well as the other agencies of the Department. We are now starting similar audits in Farmers Home Administration and Agricultural Stabilization and Conservation Service. We are also presently updating the Secretary's Memorandum which emphasizes the Secretary's commitment to timely and appropriate resolution of all audit reports.

SECURITY OF AUTOMATED INFORMATION SYSTEMS

During the past year, we have increased our audit coverage of automated data processing (ADP) operations within the Department. The proliferation of ADP equipment has resulted in a wider range of computer applications and a greater commitment of the Department's resources to ADP operations. The increased use of ADP has brought about a corresponding increase in the ADP operation's vulnerability to fraud, waste, and abuse.

In October 1980, we initiated a review of Departmental implementation of Office of Management and Budget Circular A-71 which established policies and responsibilities for the development and implementation of computer security programs by executive branch departments and agencies. The objectives of our audit are to:

- o Evaluate the guidelines and regulations established by the Department for completeness and effectiveness.
- o Determine if the guidelines and regulations established by the Department have been fully implemented.
- o Determine whether security measures adequately protect Departmental assets.
- o Evaluate the effectiveness of the management control and reporting process.

The scope of our audit will include a review of the Department's five computer centers and selected user agencies, and an evaluation of a sample of the "stand-alone" processing systems (mini-computers and remote job entry stations) maintained by various agencies.

To date, we have found problems with:

- o ADP Security Plans. Some computer centers and user agencies did not prepare annual ADP security plans.

- o Facility Access Control. Controls were not always in place or used to prevent unauthorized accesses to the center and user agency equipment areas. Some entrance and exit doors to the stand-alone processing system areas did not have locks or were not always locked when the equipment was not in use.
- o Contingency Plan. Centers and user agencies have not always developed effective contingency plans to be used in case of emergency.
- o System Access Control. System access keys (logon identifications, passwords, telephone numbers, account code security digits) were not always adequately secured. Access keys also were not changed periodically or after employees with knowledge of the keys left agency employment.
- o Management Control Process. Some agencies have not developed management control processes to assure that appropriate administrative, physical, and technical safeguards are incorporated into all new computer applications and significant modifications to existing applications. The agencies also have not evaluated the sensitivity of their computer applications on file.
- o Personnel Clearances. Some personnel did not have ADP security clearances commensurate with their job functions.

- o Physical Security. Some stand-alone processing sites did not have emergency power-off controls, fire controls, emergency exits, and the facilities were not located away from highly trafficked areas.

SYSTEMS MONITORING

Our monitoring of automated financial and management information systems continues to increase. A prime example is our audit of the Agricultural Stabilization and Conservation Service Sight Draft Accounting System (DRAC) which controls Commodity Credit Corporation sight drafts (payments) issued to producers or vendors under the various ASCS programs. These payments are distributed by approximately 2,700 State, County, and Field Offices. During Calendar Years 1977 through 1979, the DRAC system processed over 10 million sight drafts totaling about \$24 billion.

Our audit focused on the effectiveness of the manual and automated internal controls in the DRAC system. Because of the large number of distribution offices and volume of sight drafts, we made extensive use of data base analysis to identify problem areas and to determine if monetary losses resulted. We found that the Sight Draft Accounting System and related procedures were not totally effective in preventing or detecting duplicate and erroneous payments because: (1) duplicate and erroneous sight draft "issues" were entered into the system files through normal computer operations, or (2) field office personnel bypassed and overrode the system controls and did not promptly and fully research exceptions or inquiries.

As a result, over \$10 million in duplicate issue records were revealed. Based on our findings, the ASCS Management Field Office staff researched the duplicate records and found about 150 producers who had received duplicate payments totaling over \$150,000.

In addition we determined that because the management field office did not promptly notify the Federal Reserve Bank of overcharges, ASCS incurred unnecessary interest expenses of over \$50,000. The overcharges ranged from \$13,000 to \$9 million and went unresolved for periods ranging from 9 to 167 days.

We attributed these findings to:

- o The lack of controls to prevent duplicate records from entering the system.
- o Personnel bypassing and overriding internal controls.
- o Personnel not researching exception listings designed to detect duplicate and fraudulent payments.
- o Personnel making improper correction entries to the files.

ASCS agreed with the conditions in the audit report and initiated collection action on the overpayments during the audit. Currently, they are developing an automated control system to prevent duplicate and erroneous payments from reoccurring in the DRAC system.

Other systems we are monitoring include the Food and Nutrition Service's Financial Management Information System; the Federal Crop Insurance Corporation's ADP System; and various operations of the National Finance Center such as the redesign of the Department's centralized Payroll/Personnel System and the redesign of the centralized Billings and Collections System.

PROPERTY MANAGEMENT

In our previous semiannual report, we reported on our audit covering the acquisition, management, and disposition of office furniture by the Department. The following are some of the actions taken during the past six months to correct the problems described in the audit:

- o The Office of Operations and Finance has continued to monitor the National Finance Center computer-generated reports on open orders to assure that any still open, unfilled furniture orders are cancelled and that no new orders for prohibited furniture items are placed.
- o Agencies were prohibited from placing any orders for furniture from their 1981 appropriation until a detailed furniture budget was approved by OMB.
- o The Office of Operations and Finance issued strict guidelines and assigned high levels of approval authorities on the purchasing and installation of systems furniture on March 24, 1981.

We believe these actions will strengthen Department-wide property management.

MONITORING OF USSR GRAIN SUSPENSION

During this reporting period we have continued our audit task force review efforts to monitor and test compliance with the suspension of grain exports to the Soviet Union. This period we audited exporters' profit and loss statements and their net reporting positions prior to final settlement by the Commodity Credit Corporation (CCC).

The CCC-Exporter Agreement contains a provision to reduce the price on eligible contracts by an amount equal to the exporter's normal pre-tax profit margin on grain merchandising operations for the two years preceeding the suspension. OIG proposed that an independent board of accountants be appointed to establish standards and procedures under which exporters determine this margin. The Board was appointed and has since promulgated such standards and procedures.

In addition to the pre-tax profit margin deduction, the CCC-Exporter Agreement includes a provision to reflect an exporter's net short position; i.e., the difference between the volume of grain an exporter contracts to sell for export and the volume of grain he contracts to purchase for export. During the negotiations of the CCC-Exporter Agreement, OIG proposed that an exporter's net short position be deducted from the contract price of assumed contracts on the premise that if the exporter's purchases were not sufficient to cover sales, the CCC should not have to assume liability for the difference. As a result, the CCC initially proposed that a prorata share of

an exporter's net short position be deducted from the contract price. Objections by exporters to this proposal, however, caused the CCC to amend its proposal to eliminate the deduction if an exporter was in an even or a long position on any date between that of the last eligible contract and the date of the suspension, January 4, 1980.

Our current audits at the exporter level cover the following:

- o Calculations of pre-tax profit margins of exporters for the two years prior to January 4, 1980;
- o Reports of exporter net positions to determine any deductions for short positions; and
- o The eligibility and pricing of contracts on which the CCC assumed obligations.

Audit tests that we have conducted to date have found very few exporters in a net short position under the terms of the CCC-Exporter Agreement. However, we have found instances where some exporters underreported net profit margins to the CCC. Disclosures of larger profit margins reduce the amount of the CCC's final settlement. Audit adjustments to one exporter have totaled over \$500,000 with an additional \$1 million still in dispute. Based on our audits, the CCC has made final settlement with three of the thirteen exporters involved in the grain suspension. We plan to complete our audits at the remaining exporters by May 30, 1981.

In our last semiannual report, we cited several problem areas which we reported to the Commodity Credit Corporation and other Department officials. We have continued our followup on corrective actions in these areas and have reported the additional following areas to the CCC this period:

- o Erroneous adjustments to contracts assumed by the CCC of overshipments that were applied to export licenses. As a result, the CCC has adjusted its liability by about \$121,000 plus accrued interest.
- o Questionable allowances of freight increases totaling about \$166,000 to one exporter. We are continuing our review into this matter.

In addition, we recommended to the CCC that it would be cost beneficial for them to pay exporters the amounts withheld from contract settlements if the exporter provided the CCC with an irrevocable letter of credit to obtain any overpayments at the time of final settlement. The CCC accrues interest costs computed at the prime rate on funds withheld from contract settlements with exporters. These interest costs have totaled about \$3.7 million to date. Since the prime rate exceeds both the CCC and the Treasury rate to borrow funds, it would be cost beneficial for the CCC to pay the amounts withheld, subject to repayment of any excess determined by audit. The CCC has since notified exporters that a letter of credit would be accepted to cover any funds withheld should they elect such an option. To date, only two exporters have established letters of credit with the CCC.

We will be continuing our review efforts on the grain suspension, giving particular attention to the completion of exporter audits and the preparation of an overall audit report.

SECTION II

SUMMARY OF INVESTIGATIVE AND AUDIT ACTIVITIES

INVESTIGATIONS

Between October 1, 1980 and March 31, 1981, we completed 874 investigations including 748 which involved possible criminal violations. We referred 310 cases to the Department of Justice.

During the six-month period, there were 381 indictments and 235 convictions based on our investigations. Since the period of time to get court action on indictments varies widely, the 235 convictions are not necessarily related directly to the 381 indictments. Fines, recoveries, and collections resulting from our investigations during this same period totaled about \$3.7 million and claims were established for approximately \$2.3 million. The following is a breakdown by agency of indictments and convictions for the period:

<u>AGENCY</u>	<u>OCTOBER-MARCH</u>	
	<u>1980</u>	<u>1981</u>
	<u>Indict-</u>	<u>Convic-</u>
	<u>ments</u>	<u>tions</u>
Agricultural Marketing Service	0	1
Agricultural Stabilization and Conservation Service	22	26
Farmers Home Administration	19	16
Forest Service	1	0
Soil Conservation Service	1	1
Food and Nutrition Service	296	178
Animal and Plant Health Inspection Service	6	0
Food Safety and Quality Service	33	12
Federal Grain Inspection Service	1	0
Multiple Agencies (two or more USDA Agencies)	2	1
TOTALS	<u>381</u>	<u>235</u>

Examples of investigations follows:

FOOD STAMPS

- o Sixteen persons connected with retail stores in the New Orleans, Louisiana, area were arrested and indicted for purchasing food stamps for cash. One of the subjects was also charged under Louisiana State law with attempted aggravated assault because of threats made to an OIG undercover agent. (United States vs. Quyen Van Nguyen, Eastern District of Louisiana)

- o Food stamp surveys in Topeka, Wichita, and Kansas City, Kansas, have led to persons in the four cities purchasing food stamps for cash and other items. To date, 43 indictments have been issued with more expected in the near future. (United States vs. Alan Howard, District of Kansas - United States vs. William Thorn, District of Kansas - United States vs. Norris E. Peterson, Jr., District of Kansas - United States vs. Hugh F. Shea, District of Kansas - State of Kansas vs. George Poulos, Sedgwick County, Kansas)

- o A computer match to identify persons participating in the Food Stamp Program under more than one name was initiated by OIG-Audit in Chicago, Illinois. First names and birthdates of food stamp recipients were matched and extracted for initial examination. Nine cases were developed where food stamp recipients fraudulently collected benefits totaling \$231,000 under both the Food Stamp Program and Aid for Families with

Dependent Children. One person participated under four separate names and collected over \$31,000 in unauthorized payments while another, using only her real name and a single alias, defrauded the government of over \$61,000. All nine subjects have been indicted. (State of Illinois vs. Shirley Ivy, Cook County, Illinois - State of Illinois vs. Gloria Newbern, Cook County, Illinois)

- o An on-going food stamp trafficking investigation in Puerto Rico in coordination with local police has identified numerous persons purchasing food stamps for cash. During one investigation, \$26,524 in food stamps were exchanged for \$11,060 in cash and several automobiles. The subject and a confederate were arrested as they were exchanging \$7,500 in food stamps for a stolen 1980 Chevette automobile and \$2,000. This same subject was planning to purchase \$150,000 in food stamps but the transaction was not completed. The subject of another investigation was arrested after purchasing \$3,184 in food stamps for \$1,950. Further indictments are expected. (United States vs. Eduardo Irizarry Rios, District of Puerto Rico - United States vs. Jose Castro Rodriguez, District of Puerto Rico)

ANIMAL AND PLANT HEALTH INSPECTION SERVICE

- o An investigation dealing with the importation of exotic birds was jointly conducted by special agents of the United States Customs Service; Fish and Wildlife, Department of Interior; and the Office of Inspector

General, Department of Agriculture. As a result of this investigation, a bird importer, who also owns a bird quarantine station, and four other defendants were indicted on 16 counts by a Federal Grand Jury. The bird importer used fraudulent entry documents; conspired to smuggle protected birds into the U.S.; and attempted to influence a witness's testimony before a Federal Grand Jury. In addition, the owner and other defendants removed birds from the quarantine facility in violation of USDA and Custom regulations and laws. Trial is presently being conducted. (United States vs. Bert R. Slocum, et al, Southern District of Florida)

SUMMER FOOD SERVICE PROGRAM

- o The Executive Director of a youth development project conspired with the owner of a bakery to submit false invoices in order to overstate claims made in connection with the Summer Food Program. Kickbacks to the bakery owner totaled approximately \$14,800. The bakery owner pled guilty and was sentenced to three years imprisonment (suspended), placed on probation for three years, and ordered to make restitution. The Executive Director was tried, found guilty, and sentenced to two consecutive two-year prison terms. (United States vs. Earl B. Finney and United States vs. Marvin Norman, District of New Jersey)
- o A major joint undercover investigation is being conducted by the Federal Bureau of Investigation and the Inspector General, Department of Agriculture, into fraud in the USDA-funded Summer Food Service Program

for Children in New York City. During the two-year undercover investigation, agents posing as food brokers, were able to identify cash kickbacks between vendors and sponsors. In addition, a pattern of excessive false meal claims for meal reimbursement surfaced. The investigation which is continuing has resulted in 12 indictments of individuals for allegedly defrauding the government. Additional indictments are anticipated. In addition to these indictments, six individuals have previously entered guilty pleas to defrauding the government and making false statements. The trial is pending. (United States vs. Ralph Robinson, et al, Eastern District of New York)

- o A director of a church which was authorized to operate two summer feeding sites was indicted by a Federal Grand Jury on 8 counts for violations related to the Summer Feeding Program following an OIG investigation. The defendant submitted fraudulent claims for food, milk and other items totaling over \$4,000. The defendant also inflated meal counts which resulted in claims for reimbursement of over 28,000 meals that were not served, totaling over \$19,000. Checks were also issued from the program account totaling over \$7,000 for purposes other than costs incurred in the program. Trial is pending. (United States vs. Mable Delores Sellers, Northern District of Alabama, Western Division)

SPECIAL SUPPLEMENTAL FOOD PROGRAM FOR WOMEN, INFANTS AND CHILDREN

- o The owner of a supermarket in Brooklyn reported that an individual was attempting to sell WIC vouchers valued at \$2,000. An OIG agent, posing as a fence, contacted the individual and arranged the purchase. The FBI arrested the defendant in the act of selling 390 vouchers. The defendant was indicted, and the trial is pending. (United States vs. Kenneth Maxwell, Eastern District of New York)

SCHOOL LUNCH PROGRAM

- o A lunchroom manager of a high school was indicted on two counts for violations related to the School Lunch Program following an OIG investigation. The defendant submitted inflated meal counts and used assets and property of the School Lunch Program valued at \$14,000 for personal use. Trial is pending. (United States vs. Lois S. Hardin, Northern District of Alabama, Southern Division)

FARMERS HOME ADMINISTRATION

- o A builder pled guilty to one count of bribery. The builder offered a bribe to an FmHA County Supervisor who reported it to OIG. When the builder made a \$300 advance payment to the County Supervisor, the transaction was observed by OIG agents and a Deputy U.S. Marshal and an arrest was made. Sentencing is pending. (Engle Ben Palmer, Manito, Illinois)

- o A migrant worker employed in an FmHA county office under a provision of the CETA Program was convicted of stealing cash loan payments she received in her official capacity. She was sentenced to five years probation subject to the condition that she make full restitution.
(United States vs. Jeanette Clara Diggins, Southern District of Alabama)
- o An agent of a title insurance company was convicted for misappropriating government funds following an OIG investigation. The agent was diverting title insurance fees on FmHA rural rental housing projects to his own use. The funds have been recovered through the title insurance company. The agent was sentenced to five years imprisonment and fined \$2,500.
(Franklin County Common Pleas Court vs. Joseph P. Kelley)
- o An FmHA construction inspector entered into a personal business relationship with the president of a construction firm building houses under the FmHA rural housing loan program and which required FmHA inspection. In the course of his official duties, the FmHA construction inspector signed documents which he knew contained inaccurate or false information. The construction inspector subsequently pled guilty to one count of submitting a false inspection report and was sentenced to two years probation and ordered to perform 8 hours voluntary work per month for the period of his probation. (United States vs. William Tedder, Middle District of Florida)

- o A building contractor was convicted for submitting false certifications to FmHA in an attempt to ensure funding for houses he was constructing. He was sentenced to 6 months imprisonment, suspended, placed on supervised probation for 1 year, fined \$500, and required to perform 48 hours of community service. (United States vs. Gilbert B. Camunez, District of New Mexico)

SOIL CONSERVATION SERVICE

- o The Economic Development Administration (EDA) of the U.S. Department of Commerce provides funds for public jobs in areas of chronic unemployment. Because the Department lacked a local delivery system in the State of Michigan, the funds were transferred to local soil conservation districts for disbursement. Between July 1975 and December 1977, the Oscoda County Soil Conservation District received \$80,088.52 in EDA funds. The manager of the District Program diverted about \$8,300 of the funds to himself through his own "consulting firm." The manager entered a plea to a misdemeanor embezzlement information. He was fined \$1,000, sentenced to spend 120 days in a community correction center, and to serve 200 hours of community service. He was also ordered to serve three years supervised probation and make restitution of over \$2,000. (United States vs. William Lee Hartman, Eastern District of Michigan)

AGRICULTURAL STABILIZATION AND CONSERVATION SERVICE

- o A Wisconsin dairy farmer was sentenced to 30 days in jail and ordered to make restitution of \$14,207 for submitting false hay transportation claims to the Agricultural Stabilization and Conservation Service (ASCS). His claims were based on invoices listing false hay and transportation costs. (United States vs. Donald R. Johnson, Western District of Wisconsin)

- o The owner of an Iowa grain warehouse was indicted on six counts of making false statements to the government about the status of grain in his warehouse and selling grain mortgaged to the Commodity Credit Corporation. Trial is pending. (United States vs. Francis J. Muhr, Southern District of Iowa)

- o In Minnesota, a farmer received farm stored grain loans totaling \$261,444.37 and was paid over \$21,000 for storing the grain. After an ASCS inspection disclosed he was short loan collateral, the farmer admitted to OIG agents that he removed and sold more than 50,000 bushels of grain without authorization from ASCS. He was sentenced to two years imprisonment and restitution of over \$174,000. The court ordered that the farmer complete the imprisonment sentence by participating in a work release program for six months and then serving on probation. (United States vs. James G. Preiner, District of Minnesota)

- o In South Dakota, a farmer sold about 31,000 bushels of wheat mortgaged to the Commodity Credit Corporation without their authorization. He was sentenced to two years imprisonment for converting mortgaged property and making false statements to the government. (United States vs. Howard L. Franz, District of South Dakota)
- o After being charged with the resale of leaf account tobacco and other tobacco marketing violations, a tobacco corporation and its owner pled guilty to a 20 count Bill of Information in Kentucky and were fined a total of \$6,000. (United States vs. People's Tobacco Warehouse of Lebanon, Inc., et al, Western District of Kentucky)

FOOD SAFETY AND QUALITY SERVICE

- o The investigation of a "Bait and Switch" operation in Wyoming, Colorado, Montana, and elsewhere, yielded a 13-count federal indictment against one firm and seven individuals charging them with conspiracy, fraud by wire, and several violations of the Federal Meat Inspection Act. During the approximate period of July 1, 1979 and April 1, 1980, the defendants operated a series of "store-front" business to sell to the public sides of beef which were advertised in local media at bargain prices. The defendants would frequently move locations, change company ownership and company names and take other steps to avoid detection and disgruntled consumers. In furtherance of the fraudulent scheme, the defendants made advertising promises which were not kept, raised prices by using trick

computations, substituted lower grades of beef, and sold uninspected beef to unknowing consumers. Six of the individuals have pled or have been found guilty; sentences included six-month jail terms for some, up to three years probation for others, \$500 fines, and prohibitions against meat business connections without permission of the court. Trials for the remaining two defendants are pending. (United States vs. Colorado Meattoo Corporation, doing business as Mighty Fine Meats, et al, District of Wyoming)

- o A Federal Grand Jury returned a 12-count indictment against four firms and two individuals for violations of the Federal Meat Inspection Act, Mail Fraud, and Conspiracy. The principals were charged with having conspired to process meat-food products which were suitable for use as human food, without benefit of federal inspection, and the adulteration, misbranding, sale/transportation of same in commerce. The U.S. Mails were used in furtherance of the scheme. Trial is pending. (United States vs. Stanko Packing Company, et al, District of Nebraska)
- o An investigation of a meat packing plant in Cincinnati, Ohio, which was slaughtering "cancer-eye" cattle after hours resulted in six persons being charged for violations of the Federal Meat Inspection Act. A search warrant was executed by Deputy U.S. Marshals and OIG Agents. They were assisted by Compliance Officers and Veterinarians of the Food Safety and Quality Service. The search disclosed 19 cows and bulls in various

stages of slaughter without the presence of a federal meat inspector. The veterinarians determined that seven of the animals were in advanced stages of cancer and upon federal inspection would have been condemned. Some of the carcasses had been stamped to show they had passed inspection. The Vice President/Managing Officer, pled guilty to a one-count felony Information, charging unlawful slaughter with intent to defraud. Four individuals pled guilty to a one-count misdemeanor Information, charging them with the aiding and abetting of the unlawful slaughter. The remaining individual was named in a five-count indictment charging conspiracy, unlawful slaughter with intent to defraud, misbranding, and unlawful commingling of uninspected, fraudulently stamped meat with inspected, wholesome meat. Trial for this individual and sentencing of the other five persons are pending. (United States vs. Robert F. Runtz, et al, Southern District of Ohio)

- o The Vice President/Plant Manager of a meat processing firm attempted to bribe a USDA Meat Inspector by offering to pay him \$100 per week for allowing the addition of partially defatted beef tissue to beef patties without placing that information on the label of the product. The inspector reported this information and, with his corporation, OIG Agents monitored and controlled eight separate weekly payments to him of \$100 each. This information was presented to a Federal Grand Jury and an

eight-count indictment was returned against the plant official who has pled guilty to all counts. (United States vs. Benjamin Berman, Eastern District of Pennsylvania)

- o A Supervisory Veterinary Medical Officer in St. Cloud, Minnesota, pled guilty to a one-count Information charging him with falsifying his Time and Attendance Report which he was authorized to make and submit for reimbursement. The officer knowingly certified and submitted the report in which he claimed to be working on a date that he, his wife, and the president of a meat packing firm to which he was assigned, flew to Colorado on non-duty status in a corporate owned aircraft. He was sentenced to seven months in jail, of which he was required to serve 10 days, fined \$500, and placed on probation for two years. He also resigned his position. (United States vs. G. Richard Lyon, District of Minnesota)

AUDITS

During the period October 1, 1980 and March 31, 1981, the Office of Inspector General issued 243 audit reports. One hundred sixty-seven (167) of these reports had monetary values associated with them, which at the time of issuance amounted to:

Questioned Costs	\$ 8,074,000
Questioned Loans and Loan Guarantees	\$21,765,000
Savings and Management Improvements	\$52,364,000
Sanctions	<u>\$ 2,000</u>
TOTAL	<u>\$82,205,000</u>

See appendix for detailed listing of reports.

* * * * *

During the same period, we closed 343 reports, of which 196 contained monetary findings. At the time of closure, the monetary value of these findings were:

Disallowed Questioned Costs	\$ 2,500,000
Improper Loans and Loan Guarantees	\$ 1,122,000
Agreed-Upon Savings and Management Improvements	\$ 3,971,000
Sanctions	<u>\$ 1,000</u>
TOTAL	<u>\$ 7,594,000</u>

During the period October 1, 1980 through March 31, 1981, claims arising from audit reports were established in the

amount of: \$10,068,000

(\$2,316,000 from reports issued during that period, the balance from older reports)

During the same period, collections amounted to: \$ 4,419,000

(\$157,000 from reports issued during October 1, 1980 to March 31, 1981)

Collections were compromised, waived or abandoned for: \$10,203,000

(\$136,000 from reports issued during October 1, 1980 to March 31, 1981)

The table below shows the numbers of open audits in total and by age as of the beginning and as of the end of the reporting period. The figures in parentheses show the monetary values, in Million Dollars, associated with the findings as of March 31, 1981:

	<u>0-6 mos</u>	<u>7-12 mos</u>	<u>1-2 yrs</u>	<u>Over 2 yrs</u>	<u>Total</u>
As of 10-1-80	194	194	175	79	642
As of 3-31-81	191	116	199	92	598
(\$ Million)	(78)	(100)	(65)	(166)	(409)

During the last several months, we have held a number of working sessions with program personnel in the field and in Headquarters in an effort to resolve longstanding differences on old audit findings. These meetings have been very successful, and we anticipate a considerable reduction in the unresolved audit backlog to be shown in our next semiannual report.

A representative selection of our more significant audits is highlighted below:

Procurement of Food Coupons

The Food and Nutrition Service contracts with two firms, the American Bank Note Company and the United States Bank Note Company, for the production and distribution of all food coupons needed to administer the Food Stamp Program. During 1980, we conducted an audit of contracting procedures by FNS for the production of food coupons and the accountability and control over production and distribution procedures by both companies. Our audit disclosed improper accountability by FNS over the bulk shipment of food coupons to project areas, and a need for more timely reconciliation of reported deliveries and receipts. During the period October 1977 through March 1980, improper controls resulted in the disappearance of \$268,000 in food stamps while being shipped by registered mail, and \$16,000 while being shipped by armored car carriers. We recommended that FNS implement necessary accounting controls to prevent these occurrences in the future.

FOREST SERVICE

Third Party Scaling

The Forest Service uses independent third parties to measure logs and estimate the amount of merchantable wood (scaling) realized under timber sale contracts. Our audit was conducted to evaluate the controls exercised by the

Forest Service to insure the propriety of the independent scalers' work. The audit included three Regions which in 1979 sold timber valued at \$800 million of which about 78% was scaled by third parties. The audit found that:

- o The overall performance of independent scalers at specific locations was not verified. To better measure the quality of the scalers' service and better assure the accuracy of payments received from purchasers, we recommended the institution of appropriate statistical sampling methods.
- o Contract officers who are responsible for administering scaling operations did not have the authority to insure effective compliance. This often caused delays in getting independent scalers to correct noted problems. We recommended that agreements with scalers be tied to specific sales contracts and provide for contract officers to withdraw acceptance of scalers' work.
- o One Region did not verify the accuracy of log data submitted by the scalers. Since this data is subsequently used to determine the value of timber purchased, the Forest Service should be reasonably certain of its accuracy.
- o One Region conducted only five spot checks in a three year period of the scaling work at one mill which handled about 30% of the Region's log volume. Four of the five checks found conditions which did not

meet tolerance standards. This Region also allowed hazardous conditions to continue which prevented accurate scaling determinations; consequently, tolerance standards were not enforced.

The Forest Service generally concurred with our recommendations for improvement and instituted corrective actions.

The need for proper accountability is depicted by the fact that in FY 79 the Forest Service collected about \$968 million for 10.4 billion board feet of timber harvested by purchasers. Our audit of three Forest Service Regions which handled 70 percent of the FY 79 harvest disclosed that:

- o Purchasers were not always required to make advance payments or present payment bonds equivalent to the value of the estimated harvest during the next monthly accounting period. The audit found deficits in 98 of the 114 monthly periods analyzed; the deficits ranged from \$6,779 to \$616,276. These deficits represent an interest free loan to the purchaser and weaken sales administration.
- o Delays in billings and collections of amounts due from purchasers caused increased interest costs of about \$270,000 for a six month period in the three Regions audited.
- o Uniform procedures were not established to record credits to purchaser accounts. The audit identified 17 different ADP systems that were generating various types of reports.

- o Although the Forest Service planned to implement a nationwide ADP accounting system in early 1981, problems will continue unless actions are taken to correct the types of inaccuracies we found with data input.

The Forest Service agreed with our overall positions and is working to implement procedures that should improve the future accounting for timber sales.

Annually the Forest Service collects about \$5.5 million in fees from about 650 concessionaires who provide recreation opportunities for the public on National Forest lands.

During this reporting period, we completed a nationwide audit of concessionaire fee calculations. Our objectives were: (a) to determine if the concession permit fee calculations were computed in accordance with laws, regulations and Forest Service policies, (b) to evaluate Forest Service audit coverage of concessions, and (c) to review the adequacy of controls to prevent fraud, waste, abuse, and conflicts of interest.

Under the Forest Service's administration of concessionaire permits, the government lost over \$800,000 from improper fees and \$760,000 from fire damage to uninsured government buildings used by concessionaires. The losses occurred during the years 1977 through 1979.

Most of these losses occurred because the Forest Service did not administer the permits under an adequate system of accountability and audit review. Two of the larger concessions were granted permits in violation of Forest Service

policy. The Forest Service spent too little time calculating large concessionaire fees where large dollar losses occurred, and too much time applying the same complex calculations to small concessionaire permits. By reversing priorities, the Forest Service could realize \$85,652 in additional revenues annually, and reallocate \$113,250 each year to administer large concessionaire permits.

Sale of Farmer Stock Peanuts - Restricted Use of Peanut Oil

In our prior semiannual report, we reported on our audits of the sale of 1977 and 1978 crop year peanuts. A followup audit was undertaken to determine whether audit recommendations had been implemented and covered the sale of 1979 farmer stock peanuts by the Peanut and Compliance Branch of the Agricultural Stabilization and Conservation Service, Washington, D.C.

We found that the Commodity Credit Corporation (CCC) was generally following the applicable laws and regulations related to the disposition of surplus peanuts derived from the 1979 peanut price support program. However, the impartiality of the bid evaluation system could be improved by using a blind bid evaluation system so that bidder's identification will not be disclosed to the evaluation team. This will help to maintain the integrity of the peanut price support sales program. We question whether restricting peanut oil to domestic uses is the best method for disposing of peanuts not purchased for edible use. We estimated that \$2.9 million per year could be saved if CCC would allow peanut oil derived from CCC peanuts to be sold any place in the world except those countries involved in U.S. trade suspension.

Upland Cotton Program in Texas

We concluded cotton producers in West Texas counties had received unwarranted low yield disaster payments because farm yields established by ASCS were set too high. The high yields also contributed to the unusually high number of low yield payments made in this area. Payment data obtained from the Management Field Office shows that about 6,000 producers in 14 of these counties received cotton yield payments in at least 4 of the past 6 years that amounted to over \$80 million. Audit disclosed that the established yield for 426 of 751 cases tested in 6 of the 14 counties was higher than the actual harvested production in the past 3 years. This was, in part, caused by operating procedures that prevent current year yield adjustment below 90 percent of the yield established in the preceding year. We made no recommendation as ASCS issued new instructions for establishing 1981 program yields in October 20, 1980. These new procedures were incorporated into ASCS procedures on October 23, 1980. We believe the new procedures should be adequate to correct the conditions noted in this report.

In another audit, we questioned the propriety of about \$565,000 in low-yield payments to 20 cotton producers because they received about \$2 million in settlement of a lawsuit against the manufacturer of a weed killing herbicide. ASCS officials knew at the time they approved payments that the lawsuit had been filed. The Office of General Counsel (OGC) in an opinion dated August 6, 1980, ruled that the disbursement of \$565,000 in low-yield

disaster payments to the 20 producers in this case was in accord with the statute and regulations authorizing the issuance of the low-yield disaster payments under the Upland Cotton Program.

However, OGC also questioned whether prohibiting similar payments in future situations should be a policy question for the Congress or the administrative agency since there was no regulation or legislative history prohibiting this situation. We recommended strong consideration be given to initiating a legislative proposal. ASCS is now exploring various alternatives with OGC.

Failed Winter Wheat Disaster Program in South Dakota

Our audit disclosed approval of appeals for 1979 Disaster Program payments by the State ASC Committee for failed winter wheat contributed to a substantial number of improper payments being made under the Program. This began when the State Committee reversed a County Committee decision to deny failed winter wheat payments to producers who chose not to replant their failed wheat with spring wheat as required by regulations.

The reversal caused the County Committees to disburse additional payments in order to give all producers consistent treatment for the payments approved by the State Committee. Ten producers who had received disaster payments of over \$186,000 told us that they could have replanted the failed acres to spring wheat but for various reasons had not. Three of these producers said they had not replanted because they would have lost their disaster payments.

Neighbors and committeemen of 17 producers who had received disaster payments of over \$435,000 said the producers could have seeded spring wheat by the planting deadline.

FOREIGN OPERATIONS

Market Development

Audits and investigations of the National Renderers Association, a market development cooperator receiving about \$850,000 annually in Federal funds, disclosed serious management and fiscal problems at the Brussels and Tokyo offices that were affecting program operations intended to promote the export of U.S. agricultural products. These problems included weaknesses in financial controls, limited and ineffective guidance and supervision at field offices, office conditions that contributed to rumors and allegations damaging to program operations, and insufficient and ineffective action to correct identified problems.

The findings resulted in action by the Foreign Agricultural Service and National Renderers Association to assure continuance of Federal funding, including increased and improved supervision of field activities, improved follow-up on OIG reports, and major staffing changes and program direction.

Agricultural Attaches

Reviews of Agricultural Attache operations in Bangladesh and Egypt disclosed a need for USDA determinations as to the extent of desired Attache involvement in the P.L. 480 (Food for Peace) program. We noted that despite

the fact that Bangladesh and Egypt receive approximately \$350 million or 40 percent of available USDA P.L. 480 funds (Title I and III), Attache involvement in program negotiation, development, monitoring, and follow-up was limited. In essence, field program development and monitoring were left to the Agency for International Development (AID) and Attaches did not assure participating country compliance with program reporting responsibilities. Consequently, the effectiveness of program implementation, compliance with program requirements, and achievement of program objectives were reduced. Among problems noted were ineffective development and implementation of self-help measures, insufficient identification and controls over use of funds generated by the sales of P.L. 480 commodities, inefficient cargo handling resulting in commodity losses, insufficient knowledge of country storage facilities, and failure to obtain increased share of expanded commercial markets.

Our recommendations directed toward improving P.L. 480 agreements, projects, and program monitoring and compliance are being reviewed by the Foreign Agricultural Service.

Delineation of USDA Responsibilities for P.L. 480

We reported to the Deputy Under Secretary for International Affairs on the need for clarification of responsibilities between the Foreign Agricultural Service and the Office of International Cooperation and Development regarding

self-help and developmental projects of P.L. 480 agreements in order to permit effective developmental activities and avoid duplication of efforts and staffing.

The Department is preparing a position paper that is intended to specify agency responsibilities and assure that duplicative efforts are avoided.

Office of International Cooperation and Development (OICD)

Our audit disclosed that reimbursable agreements between the Agency for International Development and OICD were not being processed in an effective and expeditious manner. Consequently, several millions of dollars in program reimbursements were not received by USDA/OICD and follow-up actions were insufficient to assure identification of accounts receivable and receipt of payments.

OICD, the National Finance Center of the Department, and AID are attempting to reconcile the outstanding billings and identify transfer funds due from AID in order to permit continuance of program operations at intended levels. The agency has agreed to implement our recommendations.

Foreign Meat Inspection Program and Imports

In conjunction with Guatemala authorities and with cooperation and assistance from the Food Safety and Quality Service (FSQS) personnel, we investigated and reviewed the effectiveness of the Guatemala meat inspection program and questionable exports of beef from Guatemala to the United States.

The reviews disclosed serious weaknesses in the Guatemala program, including lack of official control over inspection certificates, packaging materials and brands, and insufficient controls with respect to transfers of product between certified and delisted meat plants in Guatemala. The investigation confirmed that some beef entering the United States was represented as being produced in plants eligible to export to the United States but contained markings of an ineligible plant. Field work in Guatemala established that transfers of beef between plants contributed to this condition.

Actions initiated by USDA included temporary restrictions on all Guatemala beef imports and close cooperation with Guatemala officials on corrective actions necessary to strengthen the local inspection program.

Weaknesses in the FSQS control over imports and security of samples held for testing were also reported to FSQS and follow-up audit work was initiated.

Export Certificates

We have performed investigations of alleged altering of export certificates involving poultry and horsemeat and have forwarded our reports to the Department of Justice. The investigations have disclosed apparent altering of export certificates. Recommendations concerning the revision of export certificates to better preclude alteration and misuse; the addition of a warning on the certificate regarding penalties for alteration or misuse; and inclusion of expiration dates are being considered by FSQS.

SECTION III

MONEY OWED TO THE DEPARTMENT OF AGRICULTURE

In accordance with a request in the report of the Senate Committee on Appropriations on the Supplemental Appropriation and Rescission Bill of 1980, the following are estimates provided by the agencies of the Department of the amount of money owed, the amount of money overdue, and the amount written-off as uncollectible during the six month reporting period:

<u>AGENCIES</u>	<u>MONEY OWED</u>	(In Thousands) <u>OVERDUE</u>	<u>WRITTEN OFF</u>
* Agricultural Stabilization and Conservation Service	\$16,220,477	\$ 54,918	\$ 135
Federal Crop Insurance Corporation	18,553	4,132	414
Food and Nutrition Service	76,001	75,887	11
Forest Service	45,413	32,168	603
*** Farmers Home Administration	43,265,000	1,900,000	2,700
** National Finance Center	18,965	10,190	-0-
*** Rural Electrification Administration	26,450,197	522	-0-
Science and Education Administration	269	132	5
Soil Conservation Service	6,646	2,736	9
TOTAL DEPARTMENT	<u>\$86,101,521</u>	<u>\$2,080,685</u>	<u>\$3,877</u>

* Includes Commodity Credit Corporation

** The National Finance Center keeps the accounts for the Food Safety and Quality Service, Federal Grain Inspection Service, Economics and Statistics Service, Agricultural Marketing Service, Office of Transportation and Animal and Plant Health Inspection Service.

*** Includes Certificates of Beneficial Ownership sold to the Federal Financing Bank but excludes Certificates of Beneficial Ownership and notes sold to other than Government.

SECTION IV

Employee Complaints ("HOTLINE")

From October 1, 1980 through March 31, 1981, the Complaint Analysis and Investigation Staff (CAIS) established 104 complaint files based on complaints received from USDA employees, the public, or forwarded from the General Accounting Office (GAO) which alleged varying degrees of fraud, waste or abuse within USDA programs. This number does not include telephone inquiries resolved over the telephone without need for the establishment of an official complaint file.

Sources of these complaints were telephone (47), mail (31), GAO (25), and walk-in (1). Four agencies accounted for 73 percent of the complaints received. They were Food and Nutrition Service (29), Farmers Home Administration (22), Food Safety and Quality Service (14), and Forest Service (11) cases.

While most complaints continue to be allegations of a noncriminal nature such as minor misconduct, general program mismanagement or waste and food stamp recipient irregularities, 25 complaints were forwarded for preliminary review to either OIG-Auditing (3) or OIG-Investigations (22). The remaining 79 cases were forwarded to their respective agencies for action.

As of March 31, 1981, final action on 51 of the FY 81 complaints has been received. Of the 51 received, 39 could not be supported by evidence or were determined to be unfounded and 12 were found to have some validity to the

allegations. Corrective action taken on those found to be valid has ranged from employee counseling to collection of \$3,780 overissuance of food stamps.

Continuing action on one FY 79 complaint has resulted in OIG-Auditing recommending to a State Director that approximately \$947,000 in FmHA disaster loans made to two individuals be repaid immediately or the loans liquidated because of audit findings that these individuals received excessive loans and they misused loan funds.

In an effort to reduce the amount of time it takes to complete action on complaints received, CAIS has instituted a follow-up system utilizing case control cards and status letters to the respective action agencies. The system is apparently working well and provides a record to alert CAIS to those agencies not properly responding to complaints.