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DOCUMENT RESUME

07986 - [C3468584]

Special Task Force for the Prevention of Fraud and Abuse.  
December 4, 1978. 12 pp. + 2 enclosures (9 pp.).

Testimony before the Senate Committee on Appropriations:  
Legislative Subcommittee; by Elmer B. Staats, Comptroller  
General.

Contact: Office of the Comptroller General.

Congressional Relevance: Senate Committee on Appropriations:  
Legislative Subcommittee.

The Government's financial assistance programs are vulnerable targets of fraud and related white-collar crimes. The identification of the extent, nature, and frequency of these illegal acts, together with strong internal controls and effective audit coverage, is essential, but several agencies reviewed were not doing enough to identify fraud. No one knows the magnitude of fraud against the Government. Agencies have not established management information systems to deal with the fraud problem; they do not know the amount of fraud in their programs nor can they estimate the potential amount of unknown fraud. Until recently, agencies have not made detection of fraud a high priority. Agencies have no assurance that personnel administering programs are referring all suspected frauds for investigation because: there are no controls to see that suspicious matters are reported; large workloads hinder identification of suspected fraud by program personnel; employees lose interest in reporting suspected frauds when followup actions are not promptly taken; and many Federal programs are administered by State, local, or private sector institutions, and Federal agencies often unjustifiably rely on those non-Federal entities to report and identify fraud. Agency investigators often do not have the background, experience, and training needed to effectively detect and identify fraud. A Special Task Force for the Prevention of Fraud has been established within GAO to evaluate the adequacy of management control systems in Federal agencies that are necessary for the prevention of fraud and to assess the adequacy of the followup and corrective actions taken on reports of auditors and investigators. (RRS)

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U. S. GENERAL ACCOUNTING OFFICE

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WITNESS LIST

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UNITED STATES GENERAL ACCOUNTING OFFICE  
Washington, D.C. 20548

FOR RELEASE ON DELIVERY  
Expected at 11:00 a.m., EST  
Monday, December 4, 1978

STATEMENT OF  
ELMER B. STAATS  
COMPTROLLER GENERAL OF THE UNITED STATES  
BEFORE THE  
SUBCOMMITTEE ON LEGISLATIVE  
SENATE APPROPRIATIONS COMMITTEE  
ON THE  
U.S. GENERAL ACCOUNTING OFFICE  
SPECIAL TASK FORCE FOR THE PREVENTION OF FRAUD AND ABUSE

Mr. Chairman and Members of the Subcommittee:

I am particularly pleased to be here today to discuss the Special Task Force for the Prevention of Fraud and Abuse that we recently established in the General Accounting Office. Our recent report entitled "Federal Agencies Can, and Should Do More to Combat Fraud in Government Programs", which I discussed in September before Senator Chiles' Subcommittee on Federal Spending Practices and Open Government, emphasizes the need for Federal agencies to prevent and detect fraud in their programs.

I think you will agree that because of the press of legislative responsibilities, the Congress generally does not approach the oversight of Federal programs in methodical

fashion. One of GAO's major functions is to cover this shortfall--to systematically examine the major operations of Federal agencies and programs. Obviously in doing this, we are often not addressing the concerns of the moment but by the same token, these efforts can and often do disclose major weaknesses deserving of congressional consideration.

Let me explain the genesis of this particular GAO audit to illustrate the point I just made. In mid-1976, which, incidentally was prior to all the General Services Administration publicity, we started some exploratory work aimed at ascertaining whether Federal agencies had instituted effective policies and procedures for combating the fraud that might exist in their programs. In doing this, we had to formulate criteria regarding the composition of an effective antifraud effort. It seemed to us that the essential elements of such an effort would include

- a set of procedures to assess the vulnerability of the programs in question. We wanted to learn if agencies had thought through the type of fraudulent schemes to which their programs were susceptible.
- the comprehensive collection and analysis of information on known incidents of fraud. The question here was whether the agencies were alert to identifying patterns or trends in the types of frauds being perpetrated.
- an aggressive effort to follow-up on instances of fraud that may have surfaced, not only to react but also

actively seek out fraudulent schemes. We wanted to know whether the agencies were "policing" as well as "investigating".

--strong leadership on the part of the Department of Justice in bringing its expertise to bear on the overall problem. Our intent here was to find out if the Department of Justice was doing what it could in assisting the agencies to combat fraud.

Our next step--an arduous and time-consuming one--was to identify and gather the evidence needed to confirm or deny the existence of the postulated problems. As discussed in the report, we reviewed activities at the Departments of Agriculture; Labor; Transportation; and Housing and Urban Development, and the Veterans Administration, General Services Administration, and Small Business Administration. We examined these agencies' policies, procedures, and records and held discussions with their officials at headquarters and field offices of five States. We also performed work at the Department of Justice's Civil and Criminal Divisions and at various U.S. Attorneys offices. We believed this kind of coverage was necessary if we were to draw broad conclusions about the matters being reviewed.

Although bright spots existed here and there with respect to an individual agency's antifraud activities, the existence of problems in the Governments' ability to fight fraud was established. Mr. Chairman, I think some of our findings bear

repeating to illustrate the magnitude of the problem.

The Government's financial assistance programs are vulnerable targets of fraud and related white-collar crimes. Identifying the extent, nature, and frequency of these illegal acts, together with strong internal controls and effective audit coverage, are essential first steps to combating and preventing them. Yet the agencies we reviewed were not doing nearly enough to identify fraud.

Federal programs involving grants, contracts, and loan guarantees are exploited through such means as

- false claims for benefits or services,
- false statements to induce contracts or secure goods or services,
- bribery or corruption of public employees and officials,
- false payment claims for goods and services not delivered, and,
- collusion involving contractors.

No one knows the magnitude of fraud against the Government. Hidden within apparently legitimate undertakings, it usually is unreported and/or undetected. The opportunities for fraud are tremendous when you consider the magnitude of some government disbursements. For example,

- The Veterans Administration has annual outlays of approximately \$18 billion in support of veteran benefits,

- The Department of Health Education and Welfare has annual outlays of approximately
  - \$109 billion in Federal and trust funds in support of the Social Security system,
  - \$10.5 billion in welfare payments
  - \$10 billion in grants to States for Medicaid, and
  - \$3 billion for student assistance.
- Federal procurements in FY-1977 were almost \$80 billion including GSA procurements for supplies and services, and DOD procurements of major weapons systems.

In our review, we found that agencies have not established management information systems to deal with the fraud problem. As a result, they do not know the amount of identified fraud in their programs, nor can they estimate the potential amount of unknown fraud. We noted, however, that individual case data was kept which could be used as a basis to formulate such a system. Without such data, agencies have no basis for establishing the level of resources needed to combat fraud, map antifraud strategies, and evaluate the scope and effectiveness of antifraud activities.

Until recently, agencies have not made fraud detection a high priority. Because their overriding concern is program execution, emphasis is on such program objectives as providing loan assistance. The low priority given to fraud detection leads to passiveness regarding potentially fraudulent situations.

None of the agencies reviewed has, until recently designated



a focal point responsible for seeking out and identifying fraud. Consequently, they generally take a reactive, rather than active, approach to fraud detection. However, a reactive approach is inadequate for detecting fraud, since there is often no specific incident to react to.

Agencies have no assurance that those personnel administering programs are referring all suspected frauds for investigation because:

- There are no controls to see that suspicious matters are reported.
- Large workloads hinder identifying suspected fraud by program personnel.
- Employees lose interest in reporting suspected frauds when follow-up actions, such as investigations and prosecutions, are not promptly taken.
- Many Federal programs are administered by State, local, or private sector institutions, and Federal agencies often unjustifiably rely on those non-Federal entities to identify and report frauds.

Agency investigators often do not have the background, experience, and training needed to effectively detect and identify fraud. About 70 percent of the staff involved in agencies reviewed had no prior experience in fraud investigations, and about 80 percent had no formal training in investigating fraud. Where investigators have such training, it was

generally limited to procurement fraud. Most investigators have also lacked the education in finance and accounting-related subjects often needed to identify fraud. Since fraud against the Government often involves examining financial documents, absence of a financial background could be detrimental to effective fraud investigations.

In our report, we also pointed out that the Department of Justice needs to provide stronger leadership. They have been slow to assist, coordinate, and monitor the antifraud efforts of Federal agencies.

In 1975, Justice, recognizing the need to deal with white-collar crime, established a white-collar crime committee. One activity of this committee was to provide guidance to agencies on combating fraud. It has met extensively with agency officials and has assisted agencies in carrying out several successful projects demonstrating the existence of fraud in their programs. However, this effort's effectiveness relies on the receptivity of the agencies to Justice's encouragement and the availability of resources Justice can devote to it. From a recent conversation with the Deputy Attorney General, I believe the Department is receptive to our recommendations.

Overall, we believe a more active, systematic approach to identifying fraud is needed. Our report contains specific recommendations to assist Federal agencies comprehensively address the fraud and abuse problem. I am hopeful that

agencies will respond to our report by taking a more active and systematic approach to identifying fraud and by following up on reports of the General Accounting Office and internal auditors.

I can report, Mr. Chairman, that some aggressive action has been taken. Some examples are:

- Before passage of legislation establishing Inspector Generals, several agencies such as Agriculture, HUD, VA, and Labor, administratively set-up an Inspector General type operation;
- Secretary Califano's "National Conference On Fraud, Abuse, And Error", scheduled for December 13 and 14,
- The White Collar Crime Seminar being sponsored by Inspector Generals from the Departments of HEW, HUD, and Agriculture.
- Among the agencies we reviewed, HUD's operational surveys are the most ambitious systematic mechanism aimed at actively seeking out and identifying fraud. The operational survey combines HUD investigators and auditors in a team which concentrates its efforts on a single HUD office. The surveys are aimed at uncovering deficiencies in program management and identifying specific irregularities, which indicate possible fraud, for investigation.

As a follow-up on our report, I have established a Special Task Force for the Prevention of Fraud and have allocated

substantial staff resources to assist the Task Force. The major responsibility of this group will be to:

- evaluate the adequacy of the management control systems in Federal agencies that are necessary for the prevention of fraud, and
- assess the adequacy of the follow-up and corrective actions taken on reports of auditors and investigators.

We believe that when systems have been properly developed and are functioning as planned, the possibility for fraud, theft, or error is greatly diminished. Where the systems do not exist, or are not being used properly, the opportunities to defraud the Government and the possibilities of error increase dramatically.

I intend to have the Task Force concentrate on agency controls over cash and receivables, inventories and supplies, and anything else of value that might be stolen or misappropriated if controls are weak. Since computer systems offer many possibilities for fraud, we will identify weaknesses in computer controls over payrolls, payments to vendors, and cash disbursements for other purposes. We will also be looking at the controls in effect to ensure that the Government gets what it pays for, and that work set out in contracts is actually performed.

The Task Force will analyze the reports of internal auditors in each agency it reviews, giving particular attention to indications of fraud or error the auditors have uncovered. Where these reports or our reviews show that

controls are weak, we will search for potentially fraudulent situations; using our own computerized data retrieval and analysis packages where practicable. At the conclusion of our work at each agency, we will prepare a report to the Congress and the agency involved, with particular emphasis on any weaknesses in management controls that would permit fraud, theft, or error to occur.

In our Financial and General Management Studies Division, we have assigned eight staff to work on a continuing basis. This "core" staff is expected to be in place and operating by early January 1979. We have also re-allocated a large number of people from our other divisions--the equivalent of 35 staff years. Based on our findings to date, we are assigning the highest priority to fraud and abuse reviews. In fact, we will pull people off other high priority work, and as our work progresses, we may find it necessary to allocate even more staff.

With the Task Force acting as the central or focal point, all our work on fraud and abuse will be brought under the umbrella of the Task Force. This procedure permits us to develop an operational capability very quickly. Task Force members are already working to coordinate fraud and abuse type reviews planned or on-going within all our divisions. By mid-January, we expect to have an initial listing of specific

reviews.

Since prevention will merit top priority in the GAO fight against fraud our work will concentrate on fixing or strengthening control weaknesses found in agency systems that permit fraud to occur. One of the best ways to prevent fraud and abuse is a series of checks and balances called internal controls. For example, when these controls operate effectively, one employee's work is usually checked by another in such a way that no one employee can abscond with agency assets without detection. The system also tends to identify error. Although no system is entirely foolproof, an effective series of checks and balances greatly decreases the likelihood that fraud and abuse will occur.

As we uncover potential fraud and abuse in our work, we will be looking for patterns that can be explored in other agencies. As individual cases of potential fraud and abuse are disclosed, we plan to work closely with staff of the newly established Inspector Generals, and the Department of Justice to assist in conducting investigations necessary for prosecution. We are still working out detailed procedures that will provide GAO periodic status reports on all cases referred to the Inspector General or Justice. Generally, we view our role as one of prevention rather than criminal investigation and prosecution.

Mr. Chairman, this summarizes our activities to date in setting-up a Special Task Force for the Prevention of Fraud. The digest of our report on fraud in Government is included as Attachment I. Our letter to Senator Chiles that announced our Special Task Force on Prevention of Fraud is included as Attachment II. I think hearings like this one are helpful. They bring problems into proper focus for management attention, and just as important, they also show the public that their Government is not only expressing concern about fraud and abuse, but is doing something about it. Your Committee is to be commended for its interest in helping curb fraud and abuse in government programs. We will be glad to respond to any questions you may have.

COMPTROLLER GENERAL'S  
REPORT TO THE CONGRESSFEDERAL AGENCIES CAN, AND  
SHOULD, DO MORE TO COMBAT  
FRAUD IN GOVERNMENT PROGRAMSD I G E S T

The Government's economic assistance programs, amounting to about \$250 billion annually, are vulnerable targets of fraud and related white-collar crimes. Identifying the extent, nature, and frequency of these illegal acts, together with strong internal controls and effective audit coverage, are essential first steps to combating and preventing them. Yet the agencies GAO reviewed--the Departments of Agriculture, Labor, Transportation, and Housing and Urban Development; and the Veterans, General Services, and Small Business Administrations--are not doing nearly enough to identify fraud.

Federal programs involving grants, contracts, and loan guarantees are exploited through such means as

- false claims for benefits or services,
- false statements to induce contracts or secure goods or services,
- bribery or corruption of public employees and officials,
- false payment claims for goods and services not delivered, or
- collusion involving contractors.

No one knows the magnitude of fraud against the Government. Hidden within apparently legitimate undertakings, it usually is unreported and/or undetected. However, all indications are that fraud is a problem of critical proportion. Department of Justice officials believe that the incidence of fraud in Federal programs ranges anywhere from 1 to 10 percent of the programs' expenditures. A former Secretary of the Department of Health, Education, and Welfare



estimated that losses under the Medicaid program alone total \$750 million annually from fraud and abuse.

The amount of suspected fraud which has surfaced confirms that the problem is severe. In 1976, for example, local jurisdictions reported to the Department of Labor that about \$38 million in alleged fraudulent unemployment insurance benefits were paid to claimants. Fraud against the Government ranks fourth among all criminal cases filed by Justice. As of March 1978, pending civil fraud suits in Justice totaled about \$250 million. According to Justice officials, this number is only a fraction of the actual amount defrauded from the Government.

Opportunities for defrauding the Government are virtually limitless because of the number, variety, and value of Federal programs. These programs, amounting to billions of dollars, involve numerous recipients, providers of goods and services, and public employees at all levels of government. The involvement of so much money, and so many people and institutions makes the Federal programs vulnerable to fraud. (See ch. 2.)

#### PASSIVE APPROACH TO DETECTION OF FRAUD

Federal agencies have not acted aggressively to detect fraud in their programs, and their practices are generally inadequate to identify potential fraud.

Agencies have not established management information systems on fraud. As a result, they do not know the amount of identified fraud in their programs, nor can they estimate the potential amount of unknown fraud. Without such data, agencies have no basis for establishing the level of resources needed to combat fraud, map antifraud strategies, and evaluate the scope and effectiveness of antifraud activities. The absence of management information systems

also precludes agencies from taking affirmative actions aimed at identifying and anticipating fraudulent activity, such as

- tracking fraud occurrences to determine trends and patterns,

- zeroing in on investigative targets,

- directing investigative resources where most needed, and

- pinpointing management procedures and program weaknesses which require strengthening to prevent recurrences of fraud. (See pp. 13 to 17.)

—Until recently, agencies have not made fraud detection a high priority. Because their overriding concern is program execution, emphasis is on such things as providing loan assistance. The low priority given to fraud detection leads to passiveness regarding potentially fraudulent situations. The Federal Highway Administration, for instance, generally views contract violations as honest mistakes, with no consideration of the underlying reasons for the violations or potential fraud. The Department of Labor regards questionable personnel and training cost reports submitted by prime sponsors as possible funds to be recovered rather than possible fraud (See pp. 17 to 19.)

—None of the agencies reviewed have, until recently, designated a focal point responsible for seeking out and identifying fraud. Consequently, they generally take a reactive, rather than active, approach to fraud detection. However, a reactive approach is inadequate for detecting fraud, since there is often no obvious incident to react to. The only ongoing, systematic mechanism to actively look for fraud in those agencies reviewed is the Department of Housing and Urban Development's operational survey—a concentrated effort by joint teams of investigators

and auditors to detect fraud and program weaknesses. The surveys have consistently uncovered numerous occurrences of suspected fraud. In other isolated instances where agencies have actively sought fraud, they also identified suspected fraud cases. (See pp. 19 to 22.)

Agencies have no assurance that those personnel administering programs are referring all suspected frauds for investigation because:

- There are no controls to see that suspicious matters are reported.
- Large workloads hinder identifying suspected fraud by program personnel. For example, only three employees were responsible for administering \$104 million in one Department of Labor program.
- Employees lose interest in reporting suspected frauds when followup actions, such as investigations and prosecutions, are not promptly taken.
- Many Federal programs are administered by State, local, or private sector institutions, and Federal agencies often unjustifiably rely on these non-Federal entities to identify and report frauds. (See pp. 23 to 26.)

Agency investigators often do not have the background, experience, and training needed to effectively detect and identify fraud. About 70 percent of them have had no prior experience in fraud investigations, and about 80 percent have had no formal training in investigating fraud. Where investigators have had such training, it was generally limited to procurement fraud. Most investigators have also lacked the education in finance and accounting-related subjects often needed to identify fraud. Since fraud against the Government often involves examining financial documents, absence of a financial background could be detrimental to

effective fraud investigations. (See pp. 26 to 28.)

JUSTICE NEEDS TO PROVIDE  
STRONGER LEADERSHIP

The Department of Justice has been slow to assist, coordinate, and monitor the anti-fraud efforts of Federal agencies. Justice has not provided agencies with

- overall management information on how fraud has occurred and can occur in their programs and
- specific, formal guidelines on which types of fraud cases will be accepted for prosecution and how they should be developed to increase the likelihood of successful prosecution.

In 1975 Justice, recognizing the need to deal with white-collar crime, established a white-collar crime committee. One activity of this committee was to provide guidance to agencies on combating fraud. It has met extensively with agency officials and has assisted agencies in carrying out several successful projects demonstrating the existence of fraud in their programs. However, this effort's effectiveness relies on persuasion and encouragement and the availability of resources Justice can devote to it. (See ch. 4.)

ACTIONS NEEDED TO ENHANCE  
THE FEDERAL EFFORT

Current national media coverage of the alleged frauds in building construction and maintenance contracting at the General Services Administration highlights Federal vulnerability to white-collar crime and the consequent need for an effective strategy to combat it.

GAO believes a more active, systematic approach to identifying fraud is needed. Heads of the Federal agencies discussed in this report should:

- Develop management information systems aimed at providing information on the most likely types and methods of fraud, including the development of techniques for estimating the magnitude of fraud in agency programs.
- Elevate fraud identification to a high agency priority.
- Take steps to make employees more aware of the potential for fraud and establish controls to see that irregularities are promptly referred to appropriate personnel.
- Fix organizational responsibility for identifying fraud.
- Provide agency investigators with appropriate fraud training. In future hirings, concentrate on recruitment of personnel with backgrounds and education more suited to the financial complexities of fraud.

The Attorney General should establish a formal plan to assist Federal agencies in combating fraud, including such procedures as:

- Working with Federal agencies to develop information on the nature of potential fraud in their programs.
- Consulting with agencies to devise systems to identify and investigate fraud.
- Advising agencies of the types of cases which will receive priority for prosecution and working with agencies to devise alternative solutions for those which will not.
- Providing feedback to Federal agency officials on program and administrative weaknesses developed by Federal prosecutors during the course of various prosecutions.

AGENCIES' COMMENTS AND RECENT ACTIONS  
TAKEN OR TO BE TAKEN

The various Federal program agencies agree that more needs to be done to effectively cope with fraud and abuse in Government programs. Most of the program agencies have said that they have recently made fraud identification a high priority and have fixed organizational responsibility for fraud detection. These agencies have also identified certain other actions they have taken or plan to take to further bolster the fraud detection effort. (See apps. I to VII.)

The Department of Justice also agrees that there is substantial room for improvement in its efforts and those of agency enforcement groups. It believes that efforts already underway such as expanding resources committed to program fraud, training investigators in fraud detection, and establishing special fraud units in U.S. attorney offices, will upgrade the Department's effectiveness. (See app. VIII.)

Some of these agencies did voice concern over certain statements contained in this report and the manner in which the report characterizes their fraud detection efforts. Chapter 5 addresses these concerns and the various agency actions taken.



COMPTROLLER GENERAL OF THE UNITED STATES  
WASHINGTON, D.C. 20548

Attachment II

October 11, 1978

The Honorable Lawton M. Chiles  
Chairman, Subcommittee on Federal Spending  
Practices and Open Government  
Committee on Governmental Affairs  
United States Senate

Dear Mr. Chairman:

Our recent report entitled "Federal Agencies Can, And Should, Do More To Combat Fraud In Government Programs," which I discussed before your Subcommittee last month, emphasizes the need for Federal agencies to prevent and detect fraud in their programs. I am hopeful that agencies will respond to our report by taking a more active and systematic approach to identifying fraud and by following up on reports of the General Accounting Office and internal auditors.

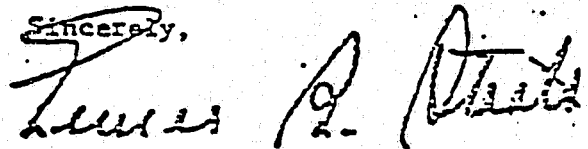
As a follow-up on our report, I have established a Special Task Force for the Prevention of Fraud and have allocated substantial staff resources to assist the Task Force over the next several months. The major responsibility of this group will be to evaluate the adequacy of the management control systems in Federal agencies that are necessary for the prevention of fraud, and to assess the adequacy of followup and corrective actions taken on reports of auditors and investigators. Where these systems have been properly developed and are functioning as planned, the possibility for fraud, theft, or error is greatly diminished. Where the systems do not exist, or are not being used properly, the opportunities to defraud the Government and the possibilities of error increase dramatically.

I intend to have the Task Force concentrate on agency controls over cash and receivables, inventories and supplies, and anything else of value that might be stolen or misappropriated if controls are weak. Since computer systems offer many possibilities for fraud, we will identify weaknesses in computer controls over payrolls, payments to vendors, and cash disbursements for other purposes. We will also be looking at the controls in effect to ensure that the Government gets what it pays for, and that work set out in contracts is actually performed.

The Task Force will analyze the reports of internal auditors in each agency it reviews, giving particular attention to indications of fraud or error the auditors have uncovered. Where these reports or our own reviews show that controls are weak, we will search for potentially fraudulent situations, using our own computerized data retrieval and analysis packages where practicable. At the conclusion of our work at each agency, we will prepare a report to the Congress and the agency involved on our work, with particular emphasis on any weaknesses in management controls that would permit fraud, theft, or error to occur. Because of the interest of your Subcommittee in this area, I will make certain that you receive copies of our reports.

A copy of this letter is being sent to the Director, Office of Management and Budget; the Chairmen, House Committee on Government Operations and Senate Committee on Governmental Affairs; the Chairman, Subcommittee on Governmental Efficiency and the District of Columbia, Senate Committee on Governmental Affairs; the Attorney General; and the Administrator of General Services.

Sincerely,

A handwritten signature in dark ink, appearing to read "Thomas A. Donohue". The signature is fluid and cursive, with the first name "Thomas" being the most prominent.

Comptroller General  
of the United States



**END**