

**UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL**

***STATEMENT OF THE HONORABLE PHYLLIS K. FONG
INSPECTOR GENERAL***

Before the
HOUSE APPROPRIATIONS SUBCOMMITTEE
ON
AGRICULTURE, RURAL DEVELOPMENT, FOOD AND DRUG
ADMINISTRATION,
AND
RELATED AGENCIES

March 1, 2006



Good morning, Mr. Chairman and Members of the Subcommittee. I thank you for inviting me to testify before you today to discuss the activities of the Office of Inspector General (OIG) and to provide information about our oversight of the Department of Agriculture's (USDA) programs and operations.

I would like to introduce the members of the OIG senior management team who are here with me today: Kathy Tighe, our new Deputy Inspector General; Robert Young, Assistant Inspector General for Audit; Mark Woods, Assistant Inspector General for Investigations; and Suzanne Murrin, Assistant Inspector General for Policy Development and Resources Management.

I welcome this opportunity to provide the Subcommittee with an overview of the highlights of our audit and investigative activity over the past year. Fiscal Year 2005 presented many difficult challenges for the USDA and our country's agricultural producers and consumers. In addition to administering programs relied upon by farmers and rural communities and managing the \$128 billion in public resources entrusted to the Department, USDA assumed significant responsibilities responding to the hurricanes that ravaged the Gulf Coast in 2005 and addressing the threat of plant and animal disease.

To best serve the Department, our Congressional oversight committees, and the general public, OIG has formally prioritized, organized, and planned our work according to three

central objectives. I will present my testimony to the Subcommittee according to the framework of these three objectives: supporting Safety, Security, and Public Health in USDA programs and operations; protecting Program Integrity as USDA provides assistance to individuals and entities; and improving the Department's Management of Public Resources.

I. Safety, Security, and Public Health

The BSE Surveillance Program and SRM Controls

We recently issued our second report focusing on the Department's efforts to establish and enforce effective, interlocking safeguards to protect producers and consumers from Bovine Spongiform Encephalopathy (BSE), commonly referred to as "mad cow disease." Our February 2006 report reviewed the Animal and Plant Health Inspection Service's (APHIS) implementation of its expanded BSE surveillance program and the Food Safety and Inspection Service's (FSIS) controls to prevent banned specified risk materials (SRM) from entering our Nation's food supply. We found that USDA made significant efforts to implement and improve the expanded surveillance program. The Department faced many challenges in a short period of time to establish the necessary processes, controls, and infrastructure needed for this massive effort. In our recent report, we discuss specific areas where we believe corrective actions were not fully effective in addressing our prior findings and recommendations on issues such as obtaining representative samples of the U.S. herd, identifying and obtaining samples from high-risk surveillance streams, and ensuring the completeness/accuracy of data. The Department

has responded to our report with immediate actions. For example, at the Secretary's direction, APHIS revised its testing protocols to provide for additional confirmatory procedures when inconclusive test results occur. Also, both APHIS and FSIS agreed with all OIG recommendations, and they have corrected, or have developed action plans to correct, the program weaknesses identified.

APHIS' Implementation of the Expanded Surveillance Plan

APHIS obtained significantly more samples for testing than it originally anticipated would be needed to achieve its stated level of confidence in estimating the prevalence of BSE in the U.S. herd. The voluntary nature of the surveillance program, however, makes it difficult to determine how successful USDA was in obtaining a representative proportion of high-risk cattle for testing. OIG found that APHIS' various statistical approaches to determining the prevalence of BSE mitigate some, but not all, of the limitations associated with its data and the agency's underlying assumptions in the design and implementation of its surveillance program. The accuracy of the underlying data is critical to the development of a future maintenance surveillance program. We recommended that APHIS disclose the limitations in its surveillance program and underlying data when it makes its final assessment of the prevalence of BSE in the U.S.

We also found that USDA needed to strengthen its processes to ensure the quality and capability of its BSE testing program, especially when inconclusive test results occur. We recommended that USDA re-evaluate and adjust its testing protocols based on its

evaluation of emerging science and strengthen its proficiency testing and quality assurance reviews at participating laboratories.

Evaluation of FSIS Processes Regarding SRMs

To examine FSIS' inspection procedures to enforce regulations to prevent risk materials in meat products, OIG reviewed the SRM plans of several meat processing facilities, observed FSIS inspections, and evaluated the effectiveness of controls during the slaughter process. FSIS technical experts assisted us in these reviews. We did not identify SRMs entering the food supply during our plant visits. However, we could not determine whether required SRM procedures were followed or were adequate due to the lack of specificity in the plans. We found that the plants lacked documentation of compliance with SRM control procedures and FSIS actions to validate such compliance.

In addition to the control issues we identified regarding SRM procedures at slaughter and processing establishments, we found that FSIS' information system could not readily provide FSIS with the data it needed to identify trends in SRM violations.

The expanded stage of USDA's BSE surveillance program is now nearing its end. Accordingly, it is important that the issues we have raised be considered as USDA completes its BSE surveillance program and reports on the prevalence of BSE in the U.S. herd. The Department has responded to our report with immediate action and agreed to address all of our findings and recommendations.

Assessing USDA Controls for Beef Exported to Japan

On January 20, 2006, Japanese officials announced that they had banned any further imports of beef products from the United States, based on the discovery that a U.S. plant had shipped a veal product containing vertebral column material that was prohibited by the terms of an agreement with Japan. On the same date, in response to Japan's decision, the Secretary announced 12 actions USDA would undertake to facilitate resuming trade. These actions include delisting and investigating the plant that exported the ineligible product, requiring a second signature on export certificates, providing training to inspection personnel on export certification, and holding meetings with inspection officials and industry representatives to reaffirm program requirements. Shortly thereafter, the Secretary requested OIG to audit the adequacy of USDA's coordination and control processes for the Beef Export Verification (BEV) program for Japan.

OIG's report, issued on February 16, 2006, concluded that the Agricultural Marketing Service (AMS) and FSIS could strengthen their controls over the BEV program by improving processes used to communicate BEV program requirements, clearly defining roles and responsibilities, and implementing additional oversight of FSIS inspection personnel. In response to our recommendations, the agencies agreed to an array of actions. AMS agreed to maintain a list of specific, export-eligible products for each facility with an approved BEV program; to systematically notify FSIS when any establishment is approved/delisted from a BEV program; and to review all establishments in the BEV program to ensure that they adhere to program requirements. FSIS agreed to

clarify the roles and responsibilities of FSIS personnel involved at each stage of the export verification process; expedite the development of export certification training; and increase supervisory oversight of the export certification process. OIG believes that the full implementation of these measures will strengthen and improve the Department's compliance with BEV program requirements.

Assessment of the Equivalence of the Canadian Beef Inspection System

Last year, my testimony discussed OIG's findings from our audit of APHIS' oversight of the importation of beef products from Canada. Our work on that audit led us to conduct an evaluation of FSIS' assessment of the equivalence of the Canadian food safety inspection system, which we issued in December 2005.

The then FSIS Administrator and the Under Secretary for Food Safety had identified concerns with the Canadian inspection system in late 2003. Our audit determined that FSIS did not fully address the issues raised by USDA officials in a timely manner. For example, in July 2003 FSIS found that Canadian inspection officials were not enforcing certain pathogen reduction and HACCP system regulations. These same types of concerns were identified again in June 2005.

At the time of our audit, FSIS did not have protocols for evaluating deficiencies in a foreign country's inspection system which could be used to question the system's equivalence to U.S. standards. In addition, FSIS had not instituted compensating controls (such as increased port-of-entry testing) to strengthen public health protections while

deficiencies were present. During the period of January 2003–May 2005, 4.4 billion pounds of Canadian processed product entered the U.S., even though FSIS officials questioned the equivalence of the Canadian inspection system.

FSIS agreed with OIG's five recommendations, which included implementing protocols to determine which deficiencies would lead FSIS to question whether a foreign country's inspection system is equivalent to the U.S. system. In response to the report, FSIS committed to develop these protocols by March 2006 and to implement them immediately thereafter.

Oversight of FSIS Recalls

For the past several years we have testified about our continuing work regarding adulterated beef product recalls. In July 2004, a Pennsylvania firm initiated a recall of approximately 170,000 pounds of ground beef patties because of mislabeling. Approximately one-fourth of this product was made, in part, from beef trim from Canada which was not eligible for import to the U.S., following the detection of a Canadian cow with BSE. In May 2005, we reported on the adequacy of FSIS' effectiveness checks and the agency's oversight of the recall. Overall, we concluded that FSIS had strengthened its procedures regarding the agency's oversight of recalls. However, we noted that FSIS personnel did not determine the amount of product purchased by firms on 26 of the 58 completed effectiveness checks. This resulted in reduced assurance that mislabeled product was completely retrieved from distribution. Agency officials concurred with the firms' assertions that the product had been removed from the marketplace. In response to

our recommendations, FSIS agreed to provide more specific direction to its personnel on identifying and evaluating the amount of product purchased.

The Subcommittee has been interested in OIG's investigation of a Pennsylvania company's recall of meat products. This remains an ongoing civil fraud investigation and we will be pleased to provide information on its resolution to the Subcommittee upon its conclusion.

WIC Fraud and Infant Formula Investigations

Fifty percent of the infants in America are beneficiaries of the Food and Nutrition Service's Women, Infants and Children (WIC) program. The main product purchased with WIC vouchers is infant formula. A growing problem is the formation of organized groups and/or individuals who have been stealing large quantities of infant formula. In addition to the economic impact the stolen infant formula has on retailers, stolen infant formula presents an enormous health and safety risk for USDA and WIC recipients. There are no controls over how the stolen infant formula is handled or maintained, and no guarantee that the infant formula is safe for consumption.

When the formula is stolen it is taken to a warehouse where a process called "cleaning the product" is performed. "Cleaning the product" means that all identifiable labeling is removed from the container and the formula is relabeled. When regular formula relabeled as iron fortified is fed to infants who require the iron fortified formula, these

infants do not receive the nutrition they need. In addition, often the expiration date is changed so there is no way to know if the formula is safe to consume.

We have had success in prosecuting WIC fraud and stolen infant formula cases. As an example, OIG conducted an investigation of two store owners in Texas who redeemed over \$1.1 million in fraudulently obtained WIC vouchers and knowingly purchased stolen infant formula. In February 2005, they pled guilty to a felony charge of engaging in money laundering in connection with WIC fraud and were sentenced to 36 months in prison. The store owners had previously pled guilty to harboring and employing foreign nationals who were residing illegally in the U.S. to manage and operate WIC stores.

Preventing the Transfer of Sensitive Technology

We continue to place a high priority on work that will assist USDA officials in strengthening the Department's defenses against threats to our Nation's food supply, production agriculture, and Federal facilities. In September 2005, we issued an audit of the Agricultural Research Service's (ARS) management controls to prevent the improper or inadvertent transfer of sensitive or dual-use research and technology to questionable individuals and entities.

We found that ARS needed to strengthen its management controls over the transfer of sensitive technology. Our most pressing concern was that ARS had not identified which of its research projects are "sensitive" or dual use, meaning those projects involving specialized knowledge that could also be exploited by individuals with questionable

intent. This problem is not limited to ARS or USDA; there are no established Governmentwide criteria. In the absence of Governmentwide criteria, we recommended that ARS seek guidance from other authoritative scientific sources (such as the Office of Science and Technology Policy), identify its sensitive or dual use research, and implement the appropriate controls (i.e., who has access, what can be disclosed).

ARS agreed with OIG's recommendations. It is currently participating in a Federal advisory board, led by the National Institutes of Health, to draft guidelines for Governmentwide usage.

Transition and Coordination of Border Inspection Activities: USDA – DHS

While APHIS' frontline inspection responsibilities at U.S. ports-of-entry and border crossings were transferred to the Department of Homeland Security's (DHS) Customs and Border Protection agency (CBP), APHIS retains responsibility for issuing policies and procedures related to agricultural border inspections. In March 2005, we issued a report which determined that APHIS could not fully ensure that the CBP-administered border inspection procedures adequately safeguards U.S. agriculture against the entry of foreign pests and diseases. APHIS and CBP also had not developed a process to promptly elevate critical issues to the Secretarial level when mutual agreement cannot be reached. OIG further found that APHIS should work with CBP/FSIS to expand controls to all incoming shipments of meat products to ensure they reach FSIS for re-inspection before entering commerce.

Many recommendations remain unresolved because of issues arising from the transfer of inspection duties from APHIS to CBP. As a result of the transfer, APHIS officials often no longer have direct control or knowledge of port operations that were transferred to CBP. APHIS officials advised OIG that efforts were underway to formalize agreements between CBP/FSIS and to provide for a systematic re-inspection of all incoming meat shipments.

We are currently engaged in a joint audit with DHS-OIG to assess CBP's agricultural inspection operations at selected port locations. Our objective is to determine the extent to which CBP is conducting agricultural inspection activities – formerly conducted by USDA – in order to minimize the introduction of harmful exotic pests and diseases in the United States.

USDA Activities Regarding Avian Influenza (AI)

Avian Influenza (AI) is a virus that infects domestic poultry, pet birds, and wild birds such as geese and ducks. APHIS protects and promotes agriculture in the United States by keeping agriculture pests and diseases such as AI from entering the country. APHIS' Veterinary Services coordinates its AI efforts with the U.S. Department of Health and Human Services and the Centers for Disease Control. OIG has an audit underway to review the effectiveness of APHIS' oversight of the AI outbreaks and determine if bio-security practices need to be improved. The audit will incorporate a review of APHIS surveillance of AI activities. We anticipate issuing our report this summer.

In response to public concerns about a potential outbreak of AI, OIG has proactively increased our coordination and investigative activities regarding the smuggling of live poultry and poultry products into the U.S. OIG considers smuggling investigations as critical to fulfilling our role in protecting the public's health and safety and the Nation's food supply. As part of our increased efforts in this area, OIG is working closely with the regulatory agencies within USDA such as APHIS and FSIS. One of our goals is to formalize protocols for the sharing of information at ports-of-entry throughout the U.S. Most smuggling investigations are worked jointly with numerous regulatory and law enforcement agencies, each with a unique mission. This collaborative effort will strike a balance between the regulatory responsibilities and the evidentiary requirements of a criminal investigation.

We currently have several ongoing investigations nationwide involving the smuggling of poultry product, which we are jointly working with DHS agencies. In January 2005, an OIG smuggling investigation resulted in a Los Angeles corporation being fined \$40,000 and placed on probation for 3 years after it pled guilty to smuggling misbranded poultry products from Korea.

OIG has also worked to ensure that our Emergency Response Team (ERT) is ready to deploy as needed in the event of an agricultural incident such as an AI outbreak. We have used the funding provided by the Subcommittee to train and provide equipment for our ERT members, and we have worked to establish partnerships at the Federal, State, and local level to ensure cooperation among all the emergency response agencies.

Improving Controls on the Use and Transfer of Biological Agents and Toxins

The Public Health Security and Bioterrorism Preparedness and Response Act of 2002 established security measures over dangerous biological agents and toxins. Within USDA, APHIS is responsible for implementing regulations governing the possession, use, and transfer of biological agents/toxins that affect animals or plants and preventing potential criminal usage. The Centers for Disease Control and Prevention (CDC) and USDA are also required to coordinate on requirements for overlap agents and toxins, which are those affecting human, as well as animal and plant health.

OIG conducted oversight work in two phases to assess USDA's compliance with the Act's security requirements. In our Phase I report issued in June 2005, we found that at the time of our review, APHIS had not fully implemented adequate controls to ensure that entities possessing biological agents and toxins submitted the proper registration records, prepared adequate laboratory security plans, and implemented safeguards for transferring listed agents and toxins.

In January 2006 we issued our Phase II report, based on OIG field visits to 10 locations where select agents/toxins were used or stored, to determine whether effective controls were in place. We found that security plans were not always based on site-specific risk assessments, may not have addressed critical requirements, and were not consistently tested or adequately reviewed. We recommended that APHIS coordinate with CDC in strengthening policies, procedures, and oversight, and monitoring of those possessing select agents and toxins. APHIS agreed with OIG's recommendation.

Assessing USDA Oversight of Genetically Engineered Organisms (GEO)

In 2005, the United States had over 123 million acres – half the worldwide total – planted with genetically engineered (GE) crops. Before GE crops can be approved for production, they must go through a field testing phase. In recent years, the GE plant acreage for which the Department has oversight responsibilities has increased markedly, from over 8,700 acres proposed to be planted in 1994 to over 92,000 acres proposed for 2005.

For the past several years, OIG has reviewed the Department's activities in this rapidly evolving area of biotechnology. In December 2005, we issued a report from our second phase of work in this area, which evaluated APHIS' oversight activities regarding the issuance of GE release permits for field testing and shipment of regulated GEOs. The review disclosed that APHIS needs a more cohesive, formal process for managing field releases of GE crops and seeds, particularly those developed for pharmaceutical and industrial purposes.

At various stages of the field release process—from the review of applications to the inspection of fields—OIG noted that improvements were needed in APHIS' regulations and management controls. OIG found that APHIS lacked basic information such as the specific location of field test sites, the protocol for growing the regulated crops, and the specific disposition of such crops at the end of field tests. At the time our audit was conducted, APHIS had not established an effective process for conducting field

inspections, tracking their outcomes, and following up on violations. APHIS regulations also need to be modified to afford it stronger enforcement capabilities and avoid financial liability in the event of unauthorized GEO releases.

In response to the audit, APHIS agreed to strengthen its regulatory process and has already taken action to address many of OIG's recommendations. Notably, APHIS agreed to consolidate and update its policies and requirements for GEO field releases; require more detailed information both prior to and during field tests; formalize its field test inspection process; and develop a comprehensive tracking system for GEO field releases.

We will continue our GEO-related work in the current fiscal year. We recently started a review to assess the Department's role in the export of GE agricultural commodities and its coordination with other Federal agencies to protect America's share of the world agricultural markets.

OIG's Emergency Response Program

OIG's Emergency Response Program (ERP) is comprised of two distinct and specialized teams, the Wildland Fire Investigation Team (WFIT) and the Emergency Response Team (ERT). The WFIT conducts independent field investigations into Forest Service firefighter fatalities during wildland fire operations as mandated by Congress (P.L. 107-203). Team members participate in required annual refresher training and additional advanced training as funding allows. The ERT is comprised of specially trained agents

who respond to agriculture-related incidents such as outbreaks of animal and plant disease and natural disasters. Additionally, the ERT is prepared and trained to conduct criminal investigations of agriculture-related incidents. The ERT and WFIT members are expanding their technical capabilities to include crime scene preservation and evidence collection, which will also support OIG regional staff during criminal investigations.

In December 2004, DHS' National Response Plan conferred upon OIG the Federal responsibility for the law enforcement response to an animal or plant disease outbreak that is determined to be a criminal (not a terrorist) act. In the event of any such outbreak, OIG would work closely with the responding agencies to ensure the proper handling and packing of any samples for testing and forensic analysis, and conduct any subsequent criminal investigation. If terrorism is suspected, OIG would notify and work jointly with the Federal Bureau of Investigation (FBI), as required by law.

Throughout 2005, ERT members participated in numerous multi-agency exercises with the FBI and other Federal, State, and local agriculture, law enforcement and emergency response agencies to improve working relationships and identify issues they may face from agricultural attacks or events. One example is our training in Ag-Terrorism with the FBI, which improved interoperability between the agencies in the event of an agro-terrorism incident. The ERT worked with several USDA offices to develop an Agriculture Weapons of Mass Destruction Incident Command Course, being proposed for the DHS' Center for Domestic Preparedness. The ERT also provided an OIG/ERT presentation at the 1st International Agro-Terrorism Symposium, sponsored by the FBI.

II: Enhancing Program Integrity and Reducing Program Vulnerabilities

Broadband Grant and Loan Programs

In the 2002 Farm Bill, Congress created a program to bring broadband technology to underserved rural areas. OIG initiated a review of the Rural Utilities Service's (RUS) implementation of the broadband loan/grant programs to determine how effectively obligated funds were being used to achieve this goal.

Although the broadband programs were intended to improve broadband service in rural communities, we found that a significant portion of the loan funds had been spent in areas that were adjacent to metropolitan areas and are primarily suburban in character. RUS has issued more than \$103.4 million in grants and loans (nearly 12% of \$895 million in program funds) to communities near metropolitan areas, including \$45.6 million in loans to 19 planned subdivisions on the outskirts of Houston. During OIG's audit, two other loan applications totaling \$26.4 million were pending for similar communities near Houston and Los Angeles. These loans were approved because RUS' definition of "rural" is too broad to distinguish between suburban and rural communities. That definition describes an eligible rural community as one with fewer than 20,000 inhabitants, but it does not take into account other factors, such as distance from urban areas, population density, or whether existing, private Internet providers could provide service to the community without a subsidized Government loan. Near Houston, affluent suburban development projects received these loans even though they were very close to

Houston's city limits and would have enjoyed broadband service without RUS' financial assistance.

We recommended that RUS clarify its definition of eligible rural area to make a more accurate distinction between suburban and rural areas. RUS responded that its loans were made according to the statutory definition and that changing it is Congress' prerogative.

We also found that RUS' administration of the broadband programs could be improved. Overall, we reviewed over \$599 million (67% of total loans and grants funded) and questioned the proper administration of over \$340 million (almost 57% of funds reviewed). Consequently, we recommended that RUS unify and improve its program administration, provide each program with specific written guidelines, recover loan and grant funds that were misspent, and adopt procedures to ensure that all future funds will be used efficiently and effectively. RUS has generally agreed with these recommendations and has taken steps to implement them.

Implementing the Improper Payments Information Act (IPIA)

The IPIA requires the head of each agency to annually review all programs and activities the agency administers to identify those that may be susceptible to significant improper payments. In FY 2005, we assessed the actions of five agencies – FSA, CSREES, RHS, RUS, RBS – to implement OCFO's strengthened guidance pertaining to IPIA. OCFO instructed agencies to perform detailed risk assessments, including transaction tests, to support their assessments of how their respective programs faced risks of improper

payments. Although we identified improvements in the agencies' risk assessments, we concluded that, in general, the five agencies had not fully implemented the guidance and could not therefore support their conclusions that the nine programs we reviewed were at low risk for improper payments. OCFO has subsequently created a working group that meets monthly to discuss requirements and due dates for various submissions to OMB. In addition, OCFO has further strengthened its guidance to agencies, making it more prescriptive.

For FY 2006, we have initiated our third series of agency IPIA reviews. We will focus on the USDA programs declared to be high risk by either the agency or the Office of Management and Budget (OMB). Our objectives are to evaluate the actions these agencies have taken to quantify the amount of improper payments; we will also assess the efforts taken to reduce the number of improper payments.

FAS: The Supplier Credit Guarantee Program

The Foreign Agricultural Service (FAS) and the Commodity Credit Corporation (CCC) administer the Supplier Credit Guarantee Program (SCGP), which promotes commercial exports of American commodities. In FY 2005, \$1.1 billion was appropriated to administer the SCGP. In FY 2005 and FY 2006, OIG opened several SCGP investigations; we continue to actively address fraud in the program. One recent investigation revealed that a U.S. exporter had inflated commodity prices to increase the USDA guarantee payment price, misrepresented the name/grade of the commodity,

forged documents, and misrepresented a foreign company as a legitimate importer of the commodity. The exporter then submitted fraudulent documents to FAS to obtain payments for the commodity. The fraud amount in this case is approximately \$1.7 million. In December 2005, the exporter pled guilty and is currently awaiting sentencing. OIG and FAS have established a working group to discuss concerns and seek improvements in the program.

Farm Programs –FSA Controls Regarding Finality Rule and Equitable Relief Decisions

FSA pays billions of dollars annually to farmers participating in its programs. Occasionally, because of errors, program participants are paid too much. Specific rules—known as the “finality rule” and “equitable relief”—have been designed to allow for the forgiveness of repayment in those cases where producers had acted in good faith, but FSA or the producer erred. Generally, the finality rule applies when FSA (and not the producer) errs, the producer has no reason to believe that the payment was in error, and more than 90 days have transpired since the producer applied for payment. Equitable relief provisions apply when the producer, making a good faith effort to comply, errs based on FSA error/misinformation or otherwise fails to fully comply with the requirements of the covered program. The 2002 Farm Bill requires that the Secretary of Agriculture submit to Congress each year a report that describes for the previous year the number of requests for equitable relief and the dispositions of the requests.

OIG conducted an audit to determine whether FSA's controls were adequate to ensure that finality rule and equitable relief determinations are tracked and accounted for properly. In our February 2006 report, we found that FSA lacked adequate management controls to track and report equitable relief and finality rule determinations on a national basis. For calendar year 2003, based on our review of the State reports of equitable relief submitted to the national office and on our detailed review of equitable relief determinations in three States, we found that the \$694,629 of approved equitable relief reported to Congress was understated by at least \$1,894,254. Further, FSA was not analyzing its equitable relief and finality rule requests to identify weaknesses in program delivery that could be remedied to prevent future needs for relief. FSA agreed with OIG's findings and is working to address these issues.

OIG Investigations into Farm Program Fraud

OIG has identified common fraud schemes used by some beneficiaries of FSA program payments; they include restructuring farming operations to avoid payment limitations and schemes involving reported acreage, yield, cause of loss, and insurability. In FY 2005, OIG investigative efforts against farm program fraud achieved 39 indictments, 53 convictions and \$43.6 million in monetary results. A recent OIG investigation revealed that a husband and wife conspired over the course of 5 years to make false statements to FSA to circumvent payment limitations and ultimately received \$1.6 million in program payments to which they were not entitled. They pled guilty and were sentenced in December 2005 to each serve 37 months in federal prison followed by 36 months' probation, and ordered to pay a total of \$1 million in restitution.

OIG also continues to vigorously pursue crop insurance fraud in the Risk Management Agency's programs. Generally, our investigations have found schemes that involve some variation of a producer conspiring to submit false claims in order to receive more indemnity payments than the producer is entitled to receive. In FY 2005, OIG investigations involving crop insurance fraud led to 2 indictments, 8 convictions and approximately \$19.3 million in monetary results. A recent investigation disclosed that a subject falsified actual production records and submissions to increase his chances of qualifying for crop insurance indemnity payments. Based upon these submissions and other false or forged documents, the subject received over \$2.1 million in crop insurance payments for crop years 1998 through 2001. He was convicted on 16 felony charges involving mail fraud and false claims, and was sentenced in June 2005 to a maximum of 87 months in prison and payment of \$2.2 million in restitution.

The Food Stamp Program: Targeting Fraud in Electronic Benefit Transfers

OIG monitors and investigates Electronic Benefit Transfer (EBT) trafficking in the Food Stamp Program (FSP) and has initiated numerous EBT investigations in collaboration with multiple Federal and local law enforcement agencies. Overall, our investigations led to 116 convictions, 115 indictments, and \$16.2 million in monetary recoveries in FY 2005.

A recent EBT trafficking case involved the owner of a small grocery store that was convicted on three counts of wire fraud and food stamp benefit trafficking. From July

1997 to October 1998, the storeowner redeemed approximately \$1.9 million in electronic food stamp benefits. The OIG investigation disclosed that the storeowner conspired with store employees in conducting thousands of illegal electronic food stamp benefit transactions. Financial analysis of the store's bank account disclosed that the storeowner allowed several employees to subsequently obtain approximately \$1.4 million in cash from the checking account. The store owner was sentenced in April 2005 to 41 months' incarceration and 24 months' probation, and ordered to pay \$801,000 in restitution.

During last year's testimony we discussed retailers moving EBT Point of Sale (POS) devices to different locations so they could illegally exchange cash for EBT benefits away from authorized stores. This movement of the POS device minimizes the chances that the retailers' trafficking activities could be detected. OIG has seen an increase in EBT fraud involving POS devices being moved to different locations. OIG has initiated numerous EBT investigations as a result of a collaborative effort with multiple Federal and local law enforcement agencies. The Food and Nutrition Service (FNS) recognizes this problem and is considering various measures to identify and correct vulnerabilities in the EBT system.

The OIG Response to Hurricanes Katrina and Rita

The Gulf Coast region suffered immense devastation from Hurricanes Katrina and Rita, and USDA is playing a significant role in Federal recovery efforts. The Department's budget for hurricane relief aid totals over \$4.5 billion to date. The President and Congressional leaders promptly requested Inspectors General to provide oversight of

Federal disaster aid programs. Our office has developed a plan for oversight of USDA's disaster relief efforts. Our goal is to ensure accountability for the Department's hurricane relief expenditures and to assist agency officials in assisting citizens and communities in the Gulf region as efficiently as possible. We are working with USDA officials and other Federal OIGs to prevent waste, fraud, and abuses from occurring in the multi-faceted relief efforts now underway.

I would like to briefly describe some of the noteworthy elements of OIG's coordinated program of Hurricane recovery-related audits, investigations, and special reviews that are now in progress. We currently have 9 audits underway pertaining to USDA actions responding to Hurricanes Katrina and Rita, and we have targeted those disaster relief programs that may be the most vulnerable to fraud. We are monitoring FNS' Disaster Food Stamp Program in Louisiana, Texas, and Mississippi to reduce fraud such as duplicate payments; reviewing administrative controls at the Rural Housing Service (RHS) regarding single and multi-family housing assistance provided to hurricane victims; assessing the impact of any waivers or revisions of administrative procedures for issuing conservation or farm program benefits to farmers who suffered economic losses from the hurricanes; and reviewing Forest Service use of FEMA funds to establish tent cities and obtain supplies for relief workers. We also anticipate reviewing RMA's processes for handling crop insurance loss claims.

On the investigative front, OIG currently has special agents assigned full-time to the Department of Justice (DOJ) Fraud Task Force located in Baton Rouge, and several

agents in our Jackson, Mississippi sub-office are working with the Mississippi Hurricane Katrina Fraud Task Force. We are working closely with the U.S. Attorney's Offices in the affected regions and currently have several open investigations based upon their referrals. We continue to identify individuals who are attempting to defraud USDA and to coordinate the sharing of that information with other Federal agencies. The majority of our cases at this time are Government benefit fraud cases involving individuals who filed false applications to obtain benefits to which they are not entitled. We anticipate that our investigations into fraud in the aftermath of the hurricanes will significantly increase as reconstruction efforts progress in the Gulf Coast region.

OIG will revise and expand our hurricane relief-related work plan as circumstances warrant. I want to assure the Subcommittee that to maximize our resources and avoid duplication, we will coordinate all of our work regarding hurricane relief with other OIGs (via the President's Council on Integrity and Efficiency's (PCIE) Homeland Security Working Group), the Government Accountability Office, and USDA officials.

III. Management of USDA's Public Resources

GIPSA's Management and Oversight of the Packers and Stockyards Programs (P&SP)

The Grain Inspection, Packers and Stockyards Administration (GIPSA) has regulatory authority within USDA to ensure a productive and competitive global marketplace for agricultural products such as livestock and poultry. In response to a Congressional

request in April 2005, we initiated an audit to evaluate GIPSA's management and oversight of P&SP to ensure anti-competitive and unfair practices in the livestock and poultry markets were accurately and effectively examined, reported, and resolved.

We concluded that GIPSA had not established an adequate control structure and environment to oversee and manage its investigative activities for P&SP. We found that P&SP had difficulties defining and tracking investigations, planning and conducting anti-competitive investigations, and making agency policy. Also, GIPSA did not fully implement agreed upon corrective actions in response to prior OIG and GAO findings. For example, P&SP did not effectively integrate economists into its investigations.

GIPSA agreed with the report's 10 recommendations. Based on its written response, the agency has completed corrective action on four recommendations and is working to complete actions on the remaining ones by September 2006. The new leadership at GIPSA has committed to take significant corrective actions to address the issues identified in OIG's report.

Implementing Research Misconduct Policies in USDA Agencies

In December 2000, the Executive Office of the President, Office of Science and Technology Policy (OSTP), issued the Federal Policy on Research Misconduct to govern all federally funded research and proposals submitted for research funding. OSTP allowed Federal agencies 1 year to implement the Government-wide policy, which included requirements to establish sound processes for identifying, adjudicating, and

taking potential administrative actions against research misconduct. In light of USDA's large investment in research – \$2.1 billion in FY 2004 – OIG assessed the Department's compliance with OSTP's policy.

In our report issued on March 31, 2005, we determined that the Department had not implemented OSTP's requirements. Except for the Forest Service, USDA agencies were operating under a patchwork of policies. Seven USDA agencies with FY 2004 research appropriations totaling an estimated \$733 million did not have official research misconduct policies. Some USDA agencies had not issued policies applicable to extramural research misconduct.

The Department generally concurred with our recommendations and agreed that a centralized oversight body for research misconduct within USDA would be established in the Office of the Undersecretary for Research, Education, and Economics. In December 2005, USDA provided OIG with information describing administrative measures which, if implemented, would substantially address our concerns.

NRCS: Compensation for Easements in the Wetlands Reserve Program (WRP)

The Natural Resources Conservation Service's (NRCS) WRP is a voluntary program that compensates landowners to take marginal agricultural land out of production and return it to wetlands through conservation easements. The current enrollment limit is 2,275,000 acres with estimated spending of \$1.5 billion over the next 10 years. The WRP statute limits compensation for easements to no more than the fair market value of the land

before the easement, less the fair market value of the land after the easement (the residual value).

We reviewed NRCS' policies and procedures for valuing WRP conservation easements and compensating landowners. We found NRCS' methods for valuing easements did not recognize residual values in determining compensation to landowners. Had residual values been recognized, we estimated that at least \$159 million in savings over the last 5 fiscal years in 13 States reviewed could have been achieved. We also found that NRCS did not have qualified appraisal staff and an adequate technical appraisal review process.

Landowners are required by law to permanently retire any existing cropland base for WRP easement areas. Such lands are not eligible for farm subsidy payments. OIG found that in 7 of 17 easement transactions reviewed in one State, the landowners continued receiving farm subsidy benefits totaling over \$800,000 for crop bases that had been purchased by the Federal Government.

NRCS agreed to develop an appraisal methodology that considers residual values in its easement valuation process and limits compensation to landowners as specified in the law. We also recommended that NRCS strengthen its appraisal process by appointing a Chief Appraiser, hiring qualified appraisal staff, and improving its procedures. NRCS and FSA also agreed to better coordinate actions to prevent improper subsidy payments.

USDA Financial Statement Audits

Effective financial management remains a priority for USDA and its agencies. Improvements are needed in the Department's financial management to allow for generating reliable and usable financial data in order to support critical decision making. We issued an unqualified opinion on USDA's financial statements for a fourth year. Although there has been significant progress in this area over the last few years, our audit disclosed weaknesses in the underlying financial process. Specifically, financial management systems and processes do not always operate as intended and deficiencies still exist in management's oversight. The inability of financial management systems to produce accurate information in a timely manner can hinder management's ability to make informed decisions on a day-to-day basis. The continuation of material weaknesses in financial management and IT security impaired the Department's ability to prepare the statements. The Department needs to improve its financial management processes to correct these weaknesses. The Department is developing corrective action plans to address the recommendations to mitigate the issues noted in the report.

Evaluating USDA Information Technology Security

The Department and its agencies have taken numerous actions to improve the security over their IT resources; however, additional actions are still needed to establish an effective security program within the Department.

In 2005, we continued to perform agency reviews. We assessed the adequacy of IT security in FSA, CSREES, and APHIS; and expanded our review of the certification and

accreditation process conducted by agencies. Though all agency systems were approved, the work performed did not fully support the agencies' assertions.

We also assessed the internal control structure of USDA's second largest data center, the OCIO/National Information Technology Center. We found that the design and functionality of the system was adequate to provide reasonable assurance that control objectives would be met. Accordingly, we rendered an unqualified opinion on the Center's internal control structure.

OIG continues to work with OCIO to strengthen the Department's IT security. In FY 2006, we plan to examine whether selected agency application system controls (manual or automated) are in place and functioning effectively to ensure transactions are properly and completely authorized and accurately processed. We also plan to conduct audits and reviews to ensure agency compliance with departmental and Federal requirements. The Department has hundreds of critical systems that are relied upon to ensure program requirements are met and financial management data is recorded in the proper timeframe, account classification, and amount. These systems also should provide management with the accurate data needed to administer the programs as intended by law.

OIG's National Computer Forensic Unit

In FY 2004, OIG received \$2 million in funding for IT operations and activities, a portion of which we used to further develop our National Computer Forensic Unit (NCFU). We appreciate the support the Subcommittee has provided to OIG in this regard, which has

enabled us to significantly enhance the NCFU's technological capabilities and expand its expertise during FY 2005. NCFU is an integral part of many of OIG's investigations. During FY 2005, NCFU provided computer analysis in 42 OIG investigations and participated in the execution of 15 search warrants.

In a recent case, NCFU assisted in an investigation of WIC trafficking and stolen infant formula which was transported interstate. During the execution of a search warrant, NCFU seized computer equipment that revealed evidence of the subject's illegal activity, which will be utilized in their criminal prosecution.

The NCFU continues to be actively involved in assisting Investigations with the analysis of EBT data. Additionally, NCFU has been working closely with our regional offices, FNS, FNS-contracted vendors, and the U.S. Attorney's Offices to identify and implement technology which would identify emerging patterns of EBT fraud. OIG's NCFU has also broadened its mission to provide support, training and advice on evidence collection and analysis to USDA agencies and is now recognized within the Department as a leader in the area of Computer Forensics. NCFU is currently working with USDA's Chief of Cyber Security to establish computer forensic protocols and best practices for other USDA forensic units.

IV. OIG's FY 2007 Budget Request

Before concluding, I would like to comment on the OIG's FY 2007 Budget Request. We in OIG have been grateful for the support of the Administration and of the Congress,

particularly the members of this Subcommittee, during consideration of our budget. You have always been appreciative of our mission and as supportive of our requests as budget realities would allow.

With your assistance and support, we have built a record of accomplishment of which we are justifiably proud: over the last three fiscal years, cost avoidances and funds returned to the Government based on our work totaled over \$1.3 billion, while our estimated appropriations for the same period were \$228 million, providing a return of \$5.82 for every dollar invested in OIG. And monetary results are only part of our job. Our investigations led to an average of 363 indictments and 353 convictions in each of the last three years. Further, in the last six months of FY 2005 alone, USDA agreed to implement 239 OIG recommendations for program improvements – these recommendations involved everything from enhancing the effectiveness of the expanded BSE Surveillance Program to addressing USDA management challenges to further improve IT security, maintain homeland security efforts, and strengthen controls over genetically engineered organisms.

As we move forward, OIG faces new and pressing demands such as providing effective oversight to USDA's handling of \$4.5 billion in assistance to the Gulf region in the wake of Hurricanes Katrina and Rita, and reviewing Department plans to deal with avian influenza. We have asked for the minimum necessary to support our already lean staffing level (the OIG has decreased in size from 777 in FY 1995 to 589 in FY 2005 – a drop of approximately 25%) and advance our ability to safely and effectively respond to emerging public health and agriculture security threats. Specifically, the President's FY

2007 request of \$82.5 million for OIG provides for an increase of \$2.2 million for mandatory pay costs and about \$700,000 to complete implementation of the expanded Emergency Response Program (ERP) initially approved in FY 2006. OIG received a first allotment of funding last fiscal year to initiate this expansion. The requested FY 2007 increase for the ERP will allow us to fully staff, train, and equip quick response teams capable of safely and effectively responding to the scene of criminal acts and other incidents that threaten the food supply, agriculture infrastructure, USDA facilities and personnel, or USDA mission areas in general.

We would be happy to provide the Subcommittee with any additional information the members and staff may find useful in considering our FY 2007 budget request.

This concludes my testimony. Thank you again for inviting me to testify before the Subcommittee, and my senior management team and I would be pleased to address any questions you may have.

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